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Supreme Court of the United States

MICROSOFT CORPORATION, *et al.*

Petitioner,

v.

DONNA VIZCAINO, *et al.*

Respondents.

ON PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

The district court issued orders clarifying the scope of the mandatory, non-opt-out class it had certified five years previously in this action, in order to ensure that all class members continued to share "distinct circumstances with the named plaintiffs." The Ninth Circuit thereafter granted a writ of mandamus overturning the district court's class clarification orders, the effect of which was to expand the scope of the potential class substantially beyond what the district court stated it intended at the time of class certification.

The questions presented for review are:

Did the court of appeals' mandamus order contravene Rule 23's grant of discretion to the district courts to manage a class, as well as the district courts' duty to ensure that a mandatory class is properly constituted and represented throughout its pendency, as confirmed most recently by this Court's decision in *Ortiz* v. *Fibreboard Corp.*, 119 S. Ct. 2295 (1999)?

Did the court of appeals significantly depart from this Court's decisions restricting mandamus to extraordinary circumstances, when it issued a writ of mandamus that forbade the district court from altering or clarifying its own prior class certification order following a remand, notwithstanding that the court of appeals' mandate did not address the scope of the class and the appellate decision was unaffected by the district court's clarification?

Did the court of appeals correctly conclude that an individual employed by an employment agency can simultaneously claim employee benefits from both the employment agency and the agency's client for which the individual performs services?

LIST OF PARTIES AND RULE 29.6 STATEMENT

The parties to the proceedings before the United States Court of Appeals for the Ninth Circuit were petitioner Microsoft Corporation, respondents Donna Vizcaino, Jon R. Waite, Mark Stout, Geoffrey Culbert, Lesley Stuart, Thomas Morgan, Elizabeth Spokoiny and Larry Spokoiny, and the United States District Court for the Western District of Washington.

Petitioner Microsoft Corporation has no parent corporation, and no publicly held company owns 10% or more of Microsoft Corporation's stock.

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ON PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
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Petitioner Microsoft Corporation respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Ninth Circuit entered in this case.

OPINIONS AND ORDER BELOW

The opinion of the court of appeals is reported at 173 F.3d 713, with a later amendment reported at 1999 WL 588878, both of which are reprinted in the attached Appendix at pages A1 through A24.[1] The Orders of the

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[1] The court of appeals filed its original opinion on May 12, 1999. On June 10, 1999, the court entered a first amended opinion, which corrected typographical errors. That opinion is the opinion reported at 173 F.3d 713. On June 24, 1999, the court of appeals entered a second amended opinion, which included three additional sentences responding to an argument made by Microsoft in its petition for rehearing and rehearing en banc. The additional sentences are reported at 1999 WL 588878, and are set forth on page A15 of the Appendix, following the phrase "F.3d at 1200."

District Court are unreported and are reprinted in the Appendix at pages A25 through A32 and A33 through A46. The court of appeals' two opinions deciding the prior appeal are reported at 120 F.3d 1006 and 97 F.3d 1187 and are reprinted at pages A47 through A85 and A86 through A125.

JURISDICTION

The judgment of the court of appeals was entered on May 12, 1999, and Petitioner's timely petition for rehearing and suggestion for rehearing en banc was denied on June 24, 1999. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

Rule 23(c)(1), Federal Rules of Civil Procedure, provides in pertinent part that the district court may enter an order determining that an action may be maintained as a class action, which order "may be conditional, and may be altered or amended [by the district court] before the decision on the merits."

The All Writs Act, Section 1651(a) of Title 28, United States Code, provides that "The Supreme Court and all courts established by Act of Congress may issue all writs necessary or appropriate in aid of their respective jurisdictions and agreeable to the usages and principles of law."

STATEMENT OF THE CASE

Upon remand following appellate proceedings that had consumed over three years, the district court issued orders clarifying the scope of the mandatory class it had originally certified five years earlier. The district court's stated purpose was to ensure that the class would encompass only those who shared the "distinct

circumstances" of the named plaintiffs, as it had envisioned and required at the time of certification, rather than extending to tens of thousands of other individuals who began providing services at Microsoft as employees of temporary agencies or as independent contractors in the years after certification, under circumstances different from the class representatives'.

Without finding any abuse of discretion in the district court's orders clarifying the scope of the class, a panel of the court of appeals granted mandamus overturning those orders and expanding the temporal and numerical scope of the potential class dramatically. *Vizcaino* v. *Microsoft Corp.*, 173 F.3d 713 & 1999 WL 588878 (9th Cir. 1999) ("*Vizcaino III*"). The panel premised its use of mandamus on its conclusion that the district court's class clarification orders had violated the mandate in *Vizcaino* v. *Microsoft Corp.*, 97 F.3d 1187 (9th Cir. 1996) ("*Vizcaino I*") and *Vizcaino* v. *Microsoft Corp.*, 120 F.3d 1006 (9th Cir. 1997) (en banc) ("*Vizcaino II*"), *cert. denied*, 118 S. Ct. 899 (1998), even though the *Vizcaino I* and *II* mandate nowhere passed upon the scope of the class and those appellate decisions would have been the same regardless of the class scope.

The court of appeals' rejection of the district court's order clarifying that the class encompassed only those "who share distinct circumstances with the named plaintiffs" (A28) enshrined a broad reading of the 1993 class order that was contrary to what the district court said it intended at the time, and ignored the effect of the passage of time on that order, including the over three years during which the earlier appeal was *sub judice*. The result is a class consisting predominantly of persons whose circumstances are not like those of the named plaintiffs. The ramifications of folding dissimilar individuals into the class are particularly grave here, because the class was certified as a mandatory class, i.e., "[t]he legal rights of absent class members . . . are

resolved regardless . . . of their consent." *Ortiz*, 119 S. Ct. at 2315.

In addition to conflicting with this Court's decisions establishing the district court's role in managing class actions, the court of appeals' use of the extraordinary writ of mandamus to prevent the district court from clarifying the scope of the class disrupts the orderly allocation of business between the district and circuit courts. Departing from the normal rule that on remand from an appeal district courts have discretion as to matters not "disposed of" on appeal, *Sprague* v. *Ticonic Nat'l Bank*, 307 U.S. 161, 168 (1939), the court of appeals overturned the class clarification order on the ground that its prior mandate "cannot be read as contemplating redefinition of the class," asserting that the class was a "central premise" and "integral element" of the *Vizcaino II* decision. *Vizcaino III* at 720, 721 (A14, A15).

Far from being "central," this "premise" arose merely from the facts that (i) plaintiffs brought the case as a class action and (ii) the mandate referred to the existence of a class. Under the court of appeals' reasoning, any appeal in a class action can now be portrayed as fixing in stone the class definition, no matter how tentative the district court's original decision.

Finally, the court of appeals' decision has far-reaching implications for the field of employment law. The issue of the employment status of temporary workers is being contested in actions throughout the nation and, as commentators have noted, the court of appeals' mandamus decision threatens to impede the orderly resolution of those cases.[2]

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[2] *See, e.g.*, Alvin D. Lurie, *Microsoft Re-re-redux: New Twist of the Eternal Triangle*, 84 Tax Notes 143 (1999); *Casey* v. *Atlantic Richfield Co.*, No. 99-06437 (C.D. Cal. filed June 24, 1999); Herman v. *Time Warner*, No. 98 Civ. 7589 (S.D.N.Y. filed Oct. 26, 1998).

The court of appeals, in a striking departure from established benefits law, ruled that persons who received employee benefits from the temporary agencies that employed them were nevertheless presumptively entitled to receive duplicate benefits from Microsoft – the client of those agencies – based on a sole factor: the title of the position the person filled while providing services for Microsoft. Although acknowledging the multi-factor test for common-law employee status of *Nationwide Mutual Insurance Co.* v. *Darden,* 503 U.S. 318, 324 (1992) and *Committee for Creative Non-Violence* v. *Reid,* 490 U.S. 730, 751-52 (1982), the court ignored the role of the agencies as employers and treated the single factor of position title as presumptively making plaintiffs common-law employees of Microsoft, entitled to "double dip" benefits from both Microsoft and their agency employers.

In addition to applying dual employment concepts from other areas of the law to produce a novel result that will affect workplaces throughout the country, this ruling also distorts the established procedures under Rule 23, by shifting to Microsoft the burden of proving that putative class members are not in fact its common-law employees but solely employees of the third-party employment agencies.

A. Background

Microsoft develops computer software and other computer products. Microsoft's business is project driven, and its need for workers fluctuates. Between 1987 and 1990, Microsoft supplemented its work force with "freelancers" who were engaged as independent contractors. The freelancers signed agreements acknowledging that they would not be eligible for Microsoft employee benefits, including the Employee Stock Purchase Plan ("ESPP"), a benefits package governed by state law that allows employees to purchase Microsoft

stock at a discount, and the Stock Purchase Plan ("SPP"), a plan governed by the Employee Retirement Income Security Act of 1974 (ERISA), 29 U.S.C. § 1001 et seq.

The named plaintiffs worked for Microsoft between 1987 and 1990; they were classified and treated as independent contractors by Microsoft, and performed a variety of jobs. Throughout that period, instead of providing freelancers with employee benefits, Microsoft generally paid them a higher hourly wage than it paid its regular employees doing similar work.

In 1990, after evaluating the work done by certain freelancers, the IRS issued several letter rulings taking the position that some of the freelancers were not independent contractors, but rather Microsoft employees, for federal employment tax purposes. These letter rulings were based on the common-law factors prescribed in an IRS regulation, 26 C.F.R. § 31.3401(c)-1(b). *See Vizcaino II* at 1009 (A52). Microsoft resolved the matter with the IRS, paying the employer's portion of the Federal Insurance Contribution Act tax for persons covered by the letter rulings. *Id.* at 1008 (A50).

Microsoft also voluntarily changed its employee classification practices. It hired as regular employees many of the independent contractors who were the subject of the IRS letter rulings. Consistent with the IRS's observation that use of temporary agencies, such as employee leasing and technical service firms, provided an acceptable option, some of the freelancers became employees of temporary help agencies having contracts with Microsoft and other companies and continued to work at Microsoft. *Id.* at 1009 (A50). The temporary agency employees, the agencies, and Microsoft acknowledged in writing their agreement that the temporary agency employees were the employees of the agencies, and would not receive benefits from Microsoft.

After the IRS issued its rulings concerning common-law employment status for employment tax

purposes, the eight named plaintiffs claimed the right to receive employee benefits from Microsoft for the time they worked at Microsoft, including the right to participate retroactively in the ESPP. In 1992, they brought this class action challenging Microsoft's refusal to provide them with benefits. On the prior appeal in this action, the Ninth Circuit en banc reversed the district court's denial of plaintiffs' claim for ESPP benefits, and directed the district court on remand to resolve "[a]ny remaining issues regarding the rights of a particular worker in the ESPP and his available remedies." *See id.* at 1015 (A66).[3]

B. The Decisions of the District Court Subject to the Writ of Mandamus

Following the remand from *Vizcaino I* and *II*, plaintiffs argued to the district court that the class should extend beyond the independent contractors whom the IRS had determined to be common-law employees for tax purposes. Rather than a class of a few hundred former freelancers whose circumstances were analogous to those of the named plaintiffs, plaintiffs asserted that the class should now embrace all persons who performed services at Microsoft as employees of temporary employment

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[3] The decisions reversing the district court's dismissal of this action were controversial. The *Vizcaino II* en banc decision was by a divided court, as was the *Vizcaino I* panel decision. Moreover, after *Vizcaino II* was decided and after this Court denied Microsoft's petition for writ of certiorari, the Tenth Circuit upheld the denial of employee benefits to plaintiffs who asserted common law status under closely analogous circumstances in a decision that is in direct conflict with the Ninth Circuit's reasoning. *Capital Cities/ABC, Inc.* v. *Ratcliff*, 141 F.3d 1405 (10th Cir.), *cert. denied*, 119 S. Ct. 173 (1998). *See also Bronk* v. *Mountain States Tel. & Tel., Inc.*, 140 F.3d 1335 (10th Cir. 1998); *Trombetta* v. *Cragin Fed. Bank for Sav. Employee Stock Ownership Plan*, 102 F.3d 1435 (7th Cir. 1996); *Abraham* v. *Exxon Corp.*, 85 F.3d 1126 (5th Cir. 1996).

agencies or as independent contractors, from 1987 to the present, regardless of when they began their work and, in the case of temporary agency employees, whether they ever worked as independent contractors.

During the more than three years the case had been pending in the court of appeals, Microsoft had followed the IRS's advice that it could avoid the problems outlined in the letter rulings by using the services of workers who were employees of temporary agencies. Microsoft's business also grew substantially during that period. Accordingly, inclusion of all temporary agency employees who have worked at Microsoft since 1987 would result in a class exponentially larger than the one envisioned by the district court when it accepted the class definition proposed by plaintiffs, subject to the express proviso that it might be later altered, as provided by Rule 23.[4]

Confronted with plaintiffs' request that the 1993 class definition be construed five years after its issuance as embracing tens of thousands of additional people whose experience was different from the named plaintiffs', the district court clarified its 1993 class certification

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[4] The class was originally certified as: "[a]ll persons employed by Microsoft Corporation in the United States who are denied employee benefits because they are considered independent contractors or employees of third-party employment agencies, but who meet the definition of employees of Microsoft Corporation under the common law." (7/21/93 Order at 15) Microsoft objected that certain issues were inappropriate for class treatment, noting that "the proposed class definition would require a legal determination for each prospective class member as to common law employee status." (4/19/93 Resp. at 4) Plaintiffs, in reply, noted that the court had the "authority under Rule 23 to separate [individual] issues" (4/26/93 Reply at 6 n.4), and the court's certification order noted, "if at a later date it appears certain questions should be decertified pursuant to 23(c)(4)(A), the court can do so" (7/21/93 Order at 13).

order. In so doing, the court stressed that it was simply making explicit the assumptions that underlay its original order. It pointed out that, as it noted in the 1993 order, each named plaintiff had been a freelancer on or before 1990, in a position reclassified by the IRS.[5] It concluded that only those similarly situated, i.e., freelancers reclassified by the IRS or "converted" by Microsoft, had claims suitable for class resolution in this action. Only those persons shared "the unique circumstances" (A37) and the "facts that characterized the named plaintiffs' relationship with Microsoft" (A41), thus ensuring that the named plaintiffs met Rule 23(a)'s requirements of commonality, typicality, and adequacy of representation. The class as clarified was limited to those who shared "an important identity" with the named plaintiffs: (i) independent contractors at Microsoft between 1987 and 1990 whose positions were reclassified by the IRS and (ii) those who had not been reclassified by the IRS, but whom Microsoft had voluntarily "converted" by transferring them to temporary help agencies, which assigned them to the same project at Microsoft. (A44)

The district court rejected plaintiffs' assertion that the class "*potentially* includes every contingent worker who ever . . . worked at Microsoft" (A39), noting that there was no factual basis to define the class so broadly because "the legal conclusions the courts have reached regarding the named plaintiffs can be assumed to apply to Microsoft's 'temps' only insofar as their circumstances match those of the plaintiffs" (A43). There was no rational basis for applying these assumptions "to other

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[5] The district court, in its original class certification order found the commonality prerequisite to be satisfied because "[t]he Internal Revenue Service has *already made a determination* that [plaintiffs] are common law employees for tax purposes," thus confirming its focus on independent contractors. (7/21/93 Order at 11) (emphasis added))

temps, whose circumstances may vary wildly, from each other and from the named plaintiffs." (A43)[6]

C. The Ninth Circuit's Decision Granting Mandamus

Plaintiffs filed a petition for mandamus, seeking an order requiring the district court to include within the 1993 class the tens of thousands of temporary agency employees who had been on assignment at Microsoft thereafter. Although neither the district court, nor Microsoft nor the IRS had ever addressed the common-law employee status of temporary workers who had not worked for Microsoft as independent contractors, the panel assigned to hear the matter granted the petition.[7]

The Court of Appeals attempted to justify its use of mandamus by taking the position that the district court's clarification of the class certification was a violation of the

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[6] On December 4, 1998, after plaintiffs' counsel filed a separate class action, with different named plaintiffs, on behalf of independent contractors and persons assigned by temporary help agencies to work at Microsoft after 1990, the district court allowed workers who "claim to have been misclassified common law employees of Microsoft within the statute of limitations tolled by the filing of this case" to intervene individually and attempt to prove their status as common-law employees, to prevent the barring of claims by the statute of limitations. (12/4/98 Order at 5)

[7] At the same time plaintiffs filed their petition for mandamus, they moved to refer the petition to the *Vizcaino I* panel. Plaintiffs' motion was granted over Microsoft's opposition; however, the panel that heard the petition was not the *Vizcaino I* panel. Judge Trott, who had dissented from the decision in favor of plaintiffs in *Vizcaino I*, was not included. Instead, Judge Hawkins, who had participated in *Vizcaino II* and favored a judgment for plaintiffs on all issues, was made the third panel member. Microsoft's motion to conform the panel to the order directing that the original *Vizcaino I* panelists participate was denied by the hybrid panel assigned to rule on the petition.

Vizcaino I and *II* mandate. Yet the class definition had been adverted to in the panel and en banc opinions in only two contexts: one, to recite verbatim the district court's definition, and the other – in the concurring and dissenting opinion – to stress that "all we decide today is whether the freelancers [i.e., the independent contractors] should have been allowed to participate in the ESPP ... during the period leading up to the 1989-90 conversion" of workers to Microsoft employee or temporary agency employee status.[8]

Having divested the district court of the discretion that Rule 23 and this Court's decisions confer on it, and without the factual record that is also the province of the district court to develop, the court of appeals held as a matter of law that anyone who performed services in any job that possesses a position title of the type filled by the freelancers prior to 1990 was presumptively a Microsoft common-law employee, and shifted the burden to Microsoft to disprove every such person's status for a period extending well over a decade.

The court of appeals thus adopted a burden-shifting presumption, based on the name of a position

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[8] For the sake of clarity, I note that all we decide today is whether the freelancers [i.e., independent contractors] should have been allowed to participate in the ESPP and the SPP during the period leading up to the 1989-90 conversion. *All agree that those freelancers who were converted into employees of outside employment agencies have no valid claim for participation in the ESPP and SPP after the date of their conversion.*

Vizcaino II at 1018-19 (O'Scannlain, J., concurring and dissenting, joined by Hall, J. and Nelson, J.) (emphasis added) (A75). No judge on the *Vizcaino II* en banc panel took issue with this statement of the scope of the decision.

alone, that temporary agency employees and independent contractors who have worked at Microsoft since 1990 have worked under the same conditions as the independent contractors found by the IRS, nearly ten years ago, to be Microsoft employees for employment tax purposes. The court of appeals ignored the disparity between the named plaintiffs' circumstances and those of the new class members.

The circuit court also treated the existence of the temporary agencies and the fact that they were the employers of the workers as irrelevant to the issue of whether those workers were also Microsoft's common-law employees. Its justification for doing so was the IRS letter rulings analyzing work performed in certain positions prior to 1990, which, the circuit court stated, "allow no exception for individuals in these positions on the ground that they may be on the payroll of employment agencies." *Vizcaino III* at 724 (A22). The court thus treated the IRS's ten-year old rulings, which addressed only whether persons were independent contractors for purposes of determining liability for employment taxes, as conclusive of the current right of others to receive contract-based employment benefits that are completely unrelated to such taxes. It also ignored the IRS's advice that Microsoft could avoid a future problem by exercising the option of using temporary agency employees.

The court bolstered its holdings by referring to other contexts in which common-law employee status has been found, without addressing either the pertinency of these cases to the issue before it or the consequences of a ruling that makes both employers liable for providing benefits to such dual status "employees" although regular employees are entitled to only a single group of benefits. This novel dual-employment holding applies both to the SPP's ERISA benefits (controlled by federal law) and ESPP benefits (governed by state law).

REASONS FOR GRANTING THE WRIT

I.

By Stripping the District Court of Its Power to Modify a Class Certification Order As a Case Progresses, the Ninth Circuit Has Disregarded Rule 23 and Undermined the Ability of District Courts to Manage Class Actions Effectively.

Rule 23(c)(1) requires that the trial court determine whether an action is appropriate for class treatment "[a]s soon as practicable after the commencement of [the] action." The need to make the certification decision early in an action is balanced by the broad authority Rule 23 gives the trial court to revisit its initial certification decision as a case progresses, right up to "the decision on the merits." Fed. R. Civ. P. 23(c)(1). *Moses H. Cone Mem'l Hosp.* v. *Mercury Constr. Corp.*, 460 U.S. 1, 12 n.14 (1983) ("The rationale behind Rule 23(c)(1) is that a certification decision should be made 'as soon as practicable,' even though later events or discoveries may mandate a different result.").

This Court has repeatedly recognized the importance to effective class action management of the trial court's ability "to adjust the class, informed by the proceedings as they unfold." *Amchem Prods., Inc.* v. *Windsor*, 521 U.S. 591, 620 (1997). *See also General Tel. Co.* v. *Falcon*, 457 U.S. 147, 160 (1982) ("Even after a certification order is entered, the judge remains free to modify it in the light of subsequent developments in the litigation."). In *Coopers & Lybrand* v. *Livesay*, 437 U.S. 463 (1978), the Court found that an order either refusing to certify or decertifying a class is not immediately appealable pursuant to the collateral-order exception to the final judgment rule because, prior to the final,

appealable judgment, "such an order is subject to revision in the District Court," *id.* at 469 (citing Fed. R. Civ. P. 23(c)(1)).

In this case the trial court's post-remand class certification decisions were proper applications of its plenary power, and its duty, to "modify [a certification order] in the light of subsequent developments in the litigation" in order to ensure "actual, not presumed, conformance with Rule 23(a)." *Falcon*, 457 U.S. at 160. The requirement that the trial court monitor a class's compliance with Rule 23's prerequisites stems from the rule's purpose of "protect[ing] absentees by blocking unwarranted or overbroad class definitions." *Amchem Prods., Inc.* v. *Windsor*, 521 U.S. 591, 620 (1997).

The Ninth Circuit, employing a contorted reading of the record, pronounced that Microsoft had waived its right to contest the class certification. But even if Microsoft had waived the matter – which it did not[9] – any such concession would be irrelevant: the immediate parties to a purported class action cannot waive the rights of absent class members. That is the point of both *Amchem Products* and *Ortiz*. *Ortiz* in particular makes clear that a

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[9] Although the court tried to justify its decision as resting on a total concession of the class scope by Microsoft, no such concession can be found in the record. The court's reliance on its assertion in *Vizcaino I* that a Magistrate Judge found that "'Microsoft conceded the fact that the named plaintiffs and the class they represent generally were common law employees'" is erroneous. *Vizcaino III* at 720 (A14) (quoting *Vizcaino I* at 1193 n.4 (A96 n.4)). In fact, the Magistrate Judge's finding was *rejected* by the District Court prior to the appeal that resulted in the *Vizcaino I* decision, and provides no support for any such concession having been made. (*See* 6/20/94 Order; 7/6/94 Order) Furthermore, *Vizcaino II* made clear that Microsoft made no such concession. The en banc panel recognized that the only "concessions" made by Microsoft concerning common law employee status were "*for purposes of this appeal.*" *Vizcaino II* at 1010 (emphasis added) (A53).

court cannot uncritically adopt the parties' views regarding the scope of the class.

Just as it was error for the lower courts in *Ortiz* to certify the class pursuant to Rule 23(b)(1) based on the parties' agreement that a limited fund existed, 119 S. Ct. at 2316, so too it was error here to forbid the district court from clarifying the scope of the class just because, at the very outset of this action, the parties may have agreed to a particular formula describing the class with respect to limited issues. Rather, the District Court has the duty to enforce "the constitutional requirement articulated in *Hansberry* v. *Lee*, 311 U.S. 32 (1940), that 'the named plaintiff at all times adequately represent the interests of absent class members.'" *Ortiz*, 119 S. Ct. at 2315 n.24 (quoting *Phillips Petroleum Co.* v. *Shutts*, 472 U.S. 797, 812 (1985)).

The district court properly excluded from the class the new generation of temporary workers who had not worked for Microsoft in an independent contractor capacity during the pertinent time period, because the named plaintiffs are not representative of such people. Each of the named plaintiffs had been an independent contractor, and the only evidence submitted by plaintiffs in support of their motion for class certification came from persons who had been independent contractors. In 1993, just after the filing of the action, most of the temporary workers at Microsoft were former independent contractors.

Four years later, after remand, the situation was far different. As the district court recognized, plaintiffs were no longer pressing this case as one about the former independent contractors, but instead were seeking to transform it into one primarily about a new and far larger group of temporary agency employees. Recognizing that, as a result of the prolonged course of the litigation, the language of its original certification order now arguably covered thousands of people who had never worked as

independent contractors for Microsoft, the district court entered a series of orders ensuring that the class would be interpreted to cover only those it had originally intended the class to encompass.

The district court's original class certification order found that Rule 23's requirement of commonality was satisfied because the IRS already had determined that each potential class member had been a common law employee of Microsoft at some point between 1986 and 1990. In its clarification order, the district court explained that "[c]learly, the court understood the proposed class to consist only of the freelance workers that the IRS determined were Microsoft employees in 1989." (A38 n.3) In keeping with its original understanding, the district court thus explained that "the class represented by the named plaintiffs is limited to the IRS-reclassified independent contractors and any work by the same workers in the same positions but as converted 'temps,'" in part because the IRS's rulings constituted "the facts that characterized the named plaintiffs' relationship with Microsoft." (A41)

Particularly in view of the four-year lapse between certification and the issuance of the mandate, it is a significant misapplication of Rule 23 to forbid the district court from clarifying the scope of the class, a misapplication that has serious implications for class management in other cases. None of the purported procedural barriers to the district court's post-remand classification orders cited by the court of appeals can withstand examination.

First, the court ruled that a district court is barred from changing a class after any decision on the merits. This ruling contradicts the plain language of the Rule, which permits alterations of a class before "*the* decision on the merits," i.e., final judgment. Fed. R. Civ. P. 23(c)(1) (emphasis added). *See Gardner* v. *Westinghouse Broad. Co.*, 437 U.S. 478, 480 n.6 (1978) ("a decision on class-

action status may be conditional, subject to alteration or amendment *prior to final* judgment, F. R. Civ. P. 23(c)(1)") (emphasis added) (internal quotation marks omitted); *International Bhd. of Teamsters* v. *United States*, 431 U.S. 324, 376 (1977) (remanding with instructions to make appropriate changes in the scope of the class prior to final judgment); *Heckler* v. *Lopez*, 469 U.S. 1082 (1984) (same); 5 Herbert B. Newberg & Alba Conte, *Newberg on Class Actions* §24.71, at 24-228 to 229 (3d ed. 1992) (Rule 23(c)(1) permits alteration of class before "final judgment"); 7B Charles Alan Wright et al., *Federal Practice and Procedure* § 1785, at 133-35 (2d ed. 1986) (decertification can occur even after "the completion of the trial on the merits"). The prior appeal, which granted partial summary judgment to plaintiffs, indisputably did not result in final judgment: rather, the case was remanded to the trial court for further proceedings.

Second, the court of appeals declared that the district court's statement at the time of class certification that it might later decertify certain questions, *see supra* note 4, was not a reservation of the right to alter the class definition, but only of a right to decertify "certain issues." *Vizcaino III* at 721 (A15). This once again misconstrues the district court's rights and duties under Rule 23. A district court need not explicitly reserve in its original certification order the power to reconsider a class certification decision to preserve such power. Rule 23(c)(1) grants district courts the power to revisit class certification at any time before final judgment.

Third, in an unusual post-decision response to Microsoft's showing, in its petition for rehearing of the mandamus decision, that it never had an opportunity to challenge the original certification and thus the panel had incorrectly found that Microsoft had a fair opportunity to contest certification, the panel issued an amended decision. *See supra* note 1. The amended decision stated that Microsoft had waived its right to contest the 1993

class certification order by not taking a "contingent cross-appeal" challenging the certification when plaintiffs filed their appeal of the district court's order granting Microsoft's motion for summary judgment and dismissing the case. *Vizcaino III*, 1999 WL 588878 (A15).

As an initial matter, Ninth Circuit precedent prior to *Vizcaino III* leaves no room for doubt that the court of appeals would *not* have entertained a contingent cross-appeal of the class certification from a defendant like Microsoft, which had prevailed on the merits before the district court. *Blake* v. *City of Los Angeles*, 595 F.2d 1367, 1385-86 (9th Cir. 1979). *See also Weil* v. *Investment/ Indicators, Research & Management, Inc.*, 647 F.2d 18, 25-27 (9th Cir. 1981); *Marks* v. *San Francisco Real Estate Bd.*, 627 F.2d 947, 952 (9th Cir. 1980) (Kennedy, J., concurring). More fundamentally, the notion that a prevailing defendant in a class action suit must, on pain of waiver, file a contingent cross-appeal raising the issue of the original class certification whenever plaintiffs appeal an order of dismissal, conflicts with views expressed elsewhere and would pointlessly clog the appellate courts. As the exhaustively researched concurring opinion of Judge Wald in *Hartman* v. *Duffey*, 19 F.3d 1459, 1464-67 (D.C. Cir. 1994) demonstrates, even the most aggressive application of contingent cross-appeal doctrine (prior to *Vizcaino III*) merely held that a circuit court had jurisdiction to entertain such a contingent cross-appeal. No court had ever held that such an appeal must be taken.

The novel rule announced by the amended panel opinion in *Vizcaino III* was a result Judge Wald in *Hartman* accurately deemed "unfair" in view of the case law, 19 F.3d at 1467, as it needlessly proliferates appeal issues and diminishes trial court flexibility. This Court rejected the principle of contingent cross appeals in the context of construing the law of the case nearly a century ago. *Ex parte Union Steamboat Co.*, 178 U.S. 317, 320 (1900).

In addition, in the present context this class action – which as it now exists is predominately for money damages – should not be certified as a mandatory class. Inasmuch as the Ninth Circuit's order purports to shield the original class certification order from further alteration, the result is a class action that runs completely contrary to this Court's rulings, including most recently the Court's explanation of the ambits of mandatory class actions in *Ortiz*.

A class action that concerns claims "predominately for money damages" must afford each absent class member both notice of the pendency of the action and "an opportunity to remove himself from the class by executing and returning an 'opt out' or 'request for exclusion' form to the court." *Phillips Petroleum Co.* v. *Shutts*, 472 U.S. 797, 812 & n.3 (1985). Although it has now become clear (as it was not at the outset) that this case is predominately for money damages, no class member has been given individual notice of the action or the opportunity to opt out of the class. The district court's rulings hereafter on damages would bind all class members without their having had the opportunity to appear or object. This is just the sort of result this Court has condemned. As this Court stated in *Ortiz*, "serious constitutional concerns [are] raised by the mandatory class resolution of individual legal claims." 119 S. Ct. at 2313.

The fact that this is a mandatory class action makes even more crucial the need for the named plaintiffs to represent the class appropriately. The district court, by clarifying that the class was limited to a "particular group of Microsoft workers, who share distinct circumstances with the named plaintiffs" (A28), was properly fulfilling its responsibility to ensure that the class met what this Court in *Ortiz* termed "the constitutional requirement . . . that 'the named plaintiff at all times adequately represent the interests of the absent class members.'" 119 S. Ct. at 2315

n.24 (quoting *Phillips Petroleum Co.* v. *Shutts*, 472 U.S. 797, 812 (1985)) (citing *Hansbury* v. *Lee*, 311 U.S. 32, 42-43 (1940)).

As the *Ortiz* Court explained, the necessity for a close fit between the class and its representatives is heightened in "mandatory class actions aggregating damage claims" because such cases "implicate the due process 'principle of general application in Anglo-American jurisprudence that one is not bound by a judgment *in personam* in a litigation in which he is not designated as a party' . . . it being 'our "deep-rooted historic tradition that everyone should have his own day in court."'" *Id.* at 2314-15 (citations omitted). Although there is a recognized exception to this general rule, which permits representation "by someone *with the same interests* who is a party" and who "adequately represent[s]" another, the conditions of the exception must be scrupulously satisfied to justify departure from this fundamental rule. *Id.* at 2315 (emphasis added). These dual concerns of constitutional dimension form the basis of the district court's duty to revisit the class scope when it appears that the interests and circumstances of the class and its representatives no longer converge.

Finally, the Ninth Circuit compounded its errors when it shifted to Microsoft the burden of proving that particular class members were not its common law employees. Not only is this ruling contrary to normal rules of burden allocation in class actions, where putative class members must establish that they are indeed part of the class, it is fundamental that a plaintiff in a breach of contract case under Washington law, *e.g.*, *Walker* v. *Herke*, 147 P.2d 255, 260 (Wash. 1944), and under ERISA, *e.g.*, *Dowden* v. *Blue Cross & Blue Shield, Inc.*, 126 F.3d 641, 644 (5th Cir. 1997), bear the burden of proving an entitlement to recovery.

II.

The Ninth Circuit's Misuse of the Writ of Mandamus Substantially Undermines District and Circuit Court Relations.

The All Writs Act grants federal courts the power to issue "all writs necessary or appropriate in aid of their respective jurisdictions and agreeable to the usages and principles of law." 28 U.S.C. §1651. In order to ensure that mandamus is used "only in extraordinary circumstances," this Court "require[s] that a party seeking issuance have no other adequate means to attain the relief he desires and that he satisfy the 'burden of showing that [his] right to issuance of the writ is "clear and indisputable."'" *Allied Chem. Corp.* v. *Daiflon, Inc.*, 449 U.S. 33, 35 (1980) (quoting *Bankers Life & Cas. Co.* v. *Holland*, 346 U.S. 379, 384 (1953) (quoting *United States* v. *Duell*, 172 U.S. 576, 582 (1899))) (citation omitted) (second alteration in original).

A traditional office of mandamus is to enforce the law of the case doctrine, *In re Blake*, 175 U.S. 114, 117 (1899), which requires a lower court to "carry . . . into execution" a decree issued by a higher court in the same case, *Sibbald* v. *United States*, 37 U.S. 488, 492 (1838). But, "[w]hile a mandate is controlling as to matters within its compass, on the remand a lower court is free as to other issues." *Sprague* v. *Ticonic Nat'l Bank*, 307 U.S. 161, 168 (1939). A lower court "is justified in considering and deciding any question left open by the mandate and opinion of [a higher court], and its decision upon such matter can only be reviewed upon a new appeal to the proper court." *Ex parte Union Steamboat Co.*, 178 U.S. 317, 319 (1900).

Neither *Vizcaino I* nor *Vizcaino II* commented on the merits of the district court's class certification order, and neither opinion contains any statement limiting the

district court's power to alter or clarify the original class certification order. Indeed, neither opinion so much as mentions Rule 23.

The court of appeals implicitly acknowledged that the mandate lacked any direction as to the scope of the class when it described the mandate as one that "cannot be read as contemplating redefinition of the class." *Vizcaino III* at 721 (A15). This Court has confined the use of mandamus to situations involving obvious disregard of a higher court's instruction, not such a nebulous post-hoc interpretation. The court of appeals' decision, if left undisturbed, would encourage circuit courts to involve themselves more often in interlocutory oversight of district court case management, completely contrary to the established structure of circuit and district court relations.

In striking contrast to the situation here, the instances in which this Court has affirmed the use of mandamus to enforce a prior appellate mandate involved the contravention of express directions. *See General Atomic Co.* v. *Felter*, 436 U.S. 493, 496 (1978) (mandamus appropriate to correct a lower court that "has again done precisely what we held that it lacked the power to do"); *La Buy* v. *Howes Leather Co.*, 352 U.S. 249, 258 (1957) (mandamus appropriate to correct a practice that the court of appeals had "for years admonished the trial judges of the [circuit]" to stop). Nothing remotely comparable occurred here: instead, the district court took great pains to attempt to follow the Ninth Circuit's mandate. The normal appeals process – not mandamus – is the appropriate means to address any issues that may remain.[10]

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[10] This Court has acknowledged that a court of appeals' construction of the scope of its own mandate is not "necessarily conclusive" and does "not . . . foreclose[ ]" this Court's construction of the earlier order. *FCC* v. *Pottsville Broad. Co.*, 309 U.S. 134, 141 (1940).

III.

The Court of Appeals' Conclusion That Temporary Workers Could Receive Benefits from Both Their Temporary Agency Employer and the Client to Which the Temporary Agency Assigns Them Significantly Clouds The Law of Employee Benefits.

Following remand, the district court devised an orderly process for examining the common law employee status of former independent contractors who worked at Microsoft as temporary agency employees. Following *Roth* v. *American Hospital Supply Corp.*, 965 F.2d 862, 866-68 (10th Cir. 1992), the trial court determined that the pertinent inquiry regarding a temporary worker's common law employee status for both the ESPP, which is governed by state law, and the SPP, which is governed by ERISA, is whether he or she is either Microsoft's or the temporary agency's employee. Similarly, in *Rho Co.* v. *Department of Revenue*, 782 P.2d 986 (Wash. 1989), the Supreme Court of Washington held that temporary agency employees are either common law employees of the temporary agency or of the entity for whom they perform work under Washington state law, which indisputably governs the availability of ESPP benefits in this case.

Ignoring both ERISA precedent and controlling Washington law, the court of appeals instead established a significant, and hitherto unrecognized, principle of dual employment: that temporary workers may claim employee benefits as common law employees from two sources simultaneously with respect to the same, single set of services. *Vizcaino III* at 722-25 (A18-23). Such a result is unprecedented and, in the context of many other ongoing controversies in this field, highly disruptive.

The court of appeals based its holding on precedent — derived from contexts different from employee benefits law, such as agency law and labor law,

where it may be necessary to assign responsibility to more than one master — that an individual can be considered to have two employers. None of those precedents, however, holds that a temporary worker can claim duplicate employee benefits, including ERISA benefits, as an employee of a temporary agency and as a common law employee of the agency's client. Indeed, one of the few cases cited by the court of appeals as support for its novel holding, *In re Earthmovers, Inc.*, 199 B.R. 62, 64-65 (Bankr. M.D. Fla. 1996), flatly rejects such a notion.

The court of appeals also relied upon inapposite IRS precedent to support its dual-employer construct[11] and ignored the provision of the Code that actually deals with the issue of a temporary agency employee's status vis-a-vis the agency's client. Specifically, I.R.C. § 414(n)(2) rejects the court of appeals' dual-employment principle in the context of temporary employees by defining a temporary, or "leased," employee as "any person who is not an employee of the [temporary agency's client]." *See* Alvin D. Lurie, *Microsoft Re-re-redux: New Twist of the Eternal Triangle,* 84 Tax Notes 143, 146-49 (1999).

The court of appeals' analysis of common law employee status is also contrary to decisions of the Court and other circuits. Although the court cited *Nationwide Mutual Insurance Co.* v. *Darden*, 503 U.S. 318, 322-23

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[11] Three of the IRS rulings cited concern the tax liability of temporary agencies and do not reach the issue of the tax liability of the temporary agency's client. Rev. Rul. 87–41, 1987–1 C.B. 296; I.R.S. Notice 87–19, 1987–1 C.B. 455 (reprinted at 14 Stand. Fed. Tax Rep. (CCH) ¶ 33,538.65); Rev. Rul. 75-41, 1975-1 C.B. 323. A fourth, though stating in dicta that clerks who worked in a concessionaire located within, but operated separately from, a department store were "employees of both" entities, actually deals with the tax liability of only the concessionaire. Rev. Rul. 66-162, 1966-1 C.B. 234. Presumably, the IRS did not seek a second set of employment taxes from the department store as well.

(1992), it reached a conclusion that does not square with *Darden*. The nub of the court of appeals' reasoning is that, because the IRS determined that some freelancers working in "specific positions" in the 1980s were Microsoft's common-law employees for employment tax purposes, any temporary agency employee working at a position from 1990 to the present that has the same name is presumptively also a common law employee of Microsoft entitled to claim Microsoft benefits, because "[t]he IRS determinations allow no exception for individuals in these positions on the ground that they may be on the payroll of employment agencies." *Vizcaino III* at 724 (A22).

The court of appeals did not apply the multi-factor common law test and its considerations as required by this Court, such as "the method of payment" (Microsoft never paid the workers), "the provision of employee benefits" (the temporary agencies provide their employees with benefits), and "the tax treatment of the hired party" (Microsoft, the temporary agencies, and the temporary agency employees, not to mention all applicable governments, treated the workers as employees of the temporary help agencies). *Community for Creative Non-Violence* v. *Reid*, 490 U.S. 730, 751-52 (1989). Other factors, such as the methods by which the agencies assign and recruit workers, the degree of the agencies' involvement in worker training and assignment, and record-keeping, are also relevant to the common law employee analysis, yet were ignored by the court of appeals. Thus, the court of appeals examined only the common law factors that were useful to its conclusion and ignored – without justification – those factors that showed that the temporary workers were not Microsoft's common law employees. Each of the factors the court of appeals ignored points to the conclusion that an individual can claim benefits from his agency or the agency's client, but not both.

The court of appeals' analysis also proceeded without an adequate factual record, underscoring the danger of a circuit court's taking over the district court's role of class management. For example, the court of appeals assumes that the conditions at Microsoft 12 years ago that led the IRS to reclassify a position remain the same today, despite Microsoft's growth, changes in the industry, changes in personnel, and all of the changes that normally take place over a lengthy period that has seen so many different business cycles. *See, e.g., In re Convergent Techs. Sec. Litig.*, 948 F.2d 507, 513 (9th Cir. 1991) (noting that the computer industry is "'a field marked by rapid technological advances'") (quoting *In re Seagate Tech. II Sec. Litig.*, 1989 Fed. Sec. L. Rep. (CCH) ¶ 94,502, at 93,202 (N.D. Cal. 1989)); Miles J. Feldman, *Toward a Clearer Standard of Protectable Information: Trade Secrets and the Employment Relationship*, 9 High Tech. L.J. 151, 157 (1994) (noting the "instability" of employment in the computer industry "[b]ecause the pace of change in the computer business and computer applications is so rapid"). The court of appeals offered no justification for this incorrect factual assumption.

CONCLUSION

Within the last year, many actions have been brought on behalf of individuals performing services as temporary agency employees or independent contractors and claiming benefits from the entity at which they performed the services. The court of appeals' decision threatens not only to perpetuate but to multiply the error of allowing temporary agency employees to reap benefits double those available to regular employees. On issues of class supervision, appellate interlocutory intervention, benefits and burden of proof, the court of appeals' decision is seriously flawed, and contrary to this Court's and other courts' decisions. This Court should grant certiorari in

the interests of (1) protecting the appropriate use of Rule 23 class actions, the significance of which was most recently confirmed by this Court in *Ortiz*, (2) protecting the traditional standards of circuit and district court relations and (3) restoring order to the law of employee benefits.

Dated: September 22, 1999

Respectfully submitted,

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APPENDIX

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

In Re DONNA VIZCAINO; JOHN R. WAITE; MARK STOUT; GEOFFREY CULBERT; LESLEY STUART; THOMAS MORGAN; ELIZABETH SPOKOINY and LARRY SPOKOINY; and the class they represent, *Plaintiffs-Petitioners,*	)	
v.	)	No. 98-71388 D.C. No. CV-93-00178-CRD
United States District Court for the Western District of Washington, *Respondent,*	)	
Microsoft Corporation and its pension and welfare benefits plans, *Defendants-Real Parties in Interest.*	)	

Petition for Writ of Mandamus to the
United States District Court
for the Western District of Washington

DONNA VIZCAINO; JOHN R. WAITE; MARK STOUT; GEOFFREY CULBERT; LESLEY STUART; THOMAS MORGAN; ELIZABETH SPOKOINY; LARRY SPOKOINY,	No. 99-35013 D.C. No. CV-93-00178-C
Plaintiffs-Appellants, v.	ORDER AMENDING OPINION AND DENYING PETITION FOR REHEARING EN BANC AND AMENDED OPINION
MICROSOFT CORPORATION, and its health and benefits plans: Health Benefit Plan, Life Insurance Plan, Short-term and Long-term Disability Plans, and Savings (401K) Plan, *Defendants-Appellees.*	

Appeal from the United States District Court
for the Western District of Washington
John C. Coughenour, District Judge, Presiding
Order Issued by Carolyn D. Dimmick, District Judge.

Submitted May 12, 1999*
San Francisco, California

Filed May 12, 1999
Amended June 10, 1999
Second Amendment June 24, 1999

* The panel unanimously finds this case suitable for decision without oral argument. Fed. R. App. P. 34(a) and 9th Cir. R. 34-4(a)(2).

Before: Stephen Reinhardt and Michael Daly Hawkins, Circuit Judges, and William W. Schwarzer,* Senior District Judge.

COUNSEL

Stephen K. Strong and David F. Stobaugh, Bendich, Stobaugh & Strong, Seattle, Washington, for the appellants-petitioners-plaintiffs.

Michael P. Monaco, Song Oswald & Mondress, Seattle, Washington, for the appellee-real party in interest.

ORDER

The opinion filed on May 12, 1999, is amended as follows: On slip opinion page 6081, line 17, please insert the following text immediately following "F.3d at 1200.":

> *Blake* v. *City of Los Angeles,* 595 F.2d 1367, 1385-86 (9th Cir. 1979), on which Microsoft relies, is inapposite, first, because the court of appeals did not adjudicate the merits of the claims of the individual class members and, second, because the defendant had contested the class certification and taken a cross-appeal. Microsoft chose not to contest the class certification in the district court (as the district court found, "[t]he only question is whether the class should be certified for all issues in the case, or just a few of the issues."). Had it done so and lost, it could have taken a contingent

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* The Honorable William W. Schwarzer, Senior United States District Judge for the Northern District of California, sitting by designation.

cross-appeal and, had it prevailed, the district court could have modified the class on remand.

The panel has voted to deny defendant/appellee/real party in interest's petition for rehearing and to reject the suggestion for rehearing en banc.

The full court has been advised of the suggestion for rehearing en banc and no active judge has requested a vote on whether to rehear the matter en banc. Fed. R. App. P. 35.

The petition for rehearing is DENIED and the suggestion for rehearing en banc is REJECTED.

OPINION

SCHWARZER, Senior District Judge:

In our prior opinions in this litigation, we held that, as common law employees, the members of a class certified by the district court were entitled to participate in Microsoft's tax qualified Employee Stock Purchase Plan ("ESPP") even though they had been told when hired that they were ineligible for such benefits and had signed contracts disclaiming them. *See Vizcaino* v. *Microsoft Corp.*, 97 F.3d 1187 (9th Cir. 1995) (*"Vizcaino* I"), *aff'd*, 120 F.3d 1006 (9th Cir. 1997) (en banc) (*"Vizcaino* II"). The certified class had been defined by the district court to include "[a]ll persons employed by Microsoft Corporation . . . who are denied employee benefits because they are considered independent contractors or employees of third-party employment agencies, but who meet the definition of employees of Microsoft Corporation under the common law." *Vizcaino* I, 97 F.3d at 1190 n.1. We reversed the district court's judgment for Microsoft and remanded for determination of "[a]ny remaining issues regarding the rights of a particular worker." *Vizcaino* II, 120 F.3d at

1015. On remand, the district court revised its prior class definition to limit the class to workers who worked for Microsoft as independent contractors between 1987 and 1990 either in positions that the Internal Revenue Service (IRS) had reclassified as in fact being common law employee positions, or in positions that Microsoft contemporaneously had voluntarily converted to temporary agency employees. It held those workers to be eligible for employee benefits for work done while independent contractors and for work subsequently performed by them in the same position as temporary employees hired through a temporary employment agency. The district court's revised class definition excludes (1) all other temporary employees hired into a position subsequent to its reclassification or conversion, and (2) all other persons who worked for Microsoft as common law employees. We must decide whether the Judge Dimmick's order fails to carry out this court's mandate.

I. FACTUAL AND PROCEDURAL BACKGROUND

The relevant facts are set forth in detail in our prior opinions. We summarize them here only to the extent necessary for this disposition.

Microsoft, in addition to having regular employees, has utilized the services of other workers whom it classified as independent contractors (sometimes called freelancers) or temporary agency employees (also called temps). Following a federal employment tax examination in 1990, the IRS determined that Microsoft had misclassified workers in various positions occupied by independent contractors and that services performed by workers in the specified positions constituted an employer-employee relationship. In response to the IRS ruling, Microsoft offered some of the workers in reclassified positions jobs as regular employees. Most of the workers, however, were given the option to "convert" to

temps or lose their working relationship with Microsoft. In addition, Microsoft voluntarily "converted" independent contractors in other positions to temps. The temporary employment agency "payrolled" these workers but in other respects the workers' relationship with Microsoft remained essentially unchanged. In the years following the reclassification and conversion, Microsoft utilized the services of numerous temps.

Plaintiffs, who were formerly independent contractors, brought this action on behalf of a class of persons employed by Microsoft who met the definition of employees under the common law but who were denied employment benefits because Microsoft considered them independent contractors or employees of third-party employment agencies. Of the various employee benefits sought by plaintiffs, only the ESPP remains at issue. Microsoft denied liability because each of the workers—though conceded to be common law employees—had signed an Independent Contractor Agreement which expressly provided that each independent contractor was responsible for his or her own benefits. The district court granted Microsoft's motion for summary judgment on two grounds: First, because the terms of the agreement barred the claim, and, second, because the terms of the ESPP had not been communicated to the workers and therefore could not have become a part of their contract.

We reversed, holding that through its express incorporation of § 423 of the Internal Revenue Code, *see* 26 U.S.C. § 423 (1994), which requires that qualifying stock purchase plans permit all common law employees to participate, Microsoft's ESPP extended eligibility to all common law employees. *See Vizcaino* I, 97 F.3d at 1197. The plaintiff class was therefore afforded the same options to acquire stock as all other employees. *See id.* We remanded for "the determination of any questions of individual eligibility for benefits that may remain following issuance of this opinion and for calculation of the damages

or benefits due the various class members." *Id.* at 1200; *see also Vizcaino* II, 120 F.3d at 1015 ("Any remaining issues regarding the rights of a particular worker in the ESPP and his available remedies must be decided by the district court upon remand.").

On remand, the district court, on February 13, 1998, issued its "Order Regarding Scope of Remand." It denied Microsoft's motion for clarification of the composition of the class, rejecting its contention that the class definition excluded those plaintiffs who were temps and whose claims arose post-conversion (some but not all of whom had worked as independent contractors pre-conversion). The court concluded that "the plaintiff class will remain as defined in its original certification order [of July 21, 1993] until the issue of whether post-conversion plaintiffs are common law employees is presented."

Following the February 13 order, Microsoft renewed its motion to amend the class certification, asking the court to "certify subclasses for the question of who is a common law employee." By order of July 15, 1998, the district court denied Microsoft's motion but "clarified" the class definition, limiting the class to

> all Microsoft workers who, like all the named plaintiffs, worked as independent contractors between 1987 and 1990 and whose positions were reclassified as employee positions after the IRS reviewed them. This . . . includes the claims brought by the same workers for their work after 1990, when many of them, including four named plaintiffs, were transferred to temporary employment agencies. This is the scope of the plaintiff class.

The court explained that the class had to be clarified because it could only include "the named plaintiffs and

those similarly situated, both before and after conversion to temporary employment." The new definition excluded from the class other groups of potential claimants who were not reclassified by the IRS or converted by Microsoft, i.e., temps hired post-conversion into reclassified or converted positions, and all other common law employees not treated as such by Microsoft.

The July order also granted partial summary judgment for plaintiffs (it is unclear whether the order included only named plaintiffs or also the members of the redefined class). Based on Microsoft's concession, the court found these plaintiffs to have been common law employees while working as independent contractors in positions later reclassified by the IRS. In addition, it found that most plaintiffs who had subsequently been converted into temps were also common law employees entitled to ESPP participation during their time as temps. The court reasoned that the issue is "not *whether* a worker is an employee or an independent contractor; the question is *which* company is the workers' employer (Microsoft or a temporary agency)." Using a five-factor test it had devised (considering recruitment, training, duration of employment, right to assign additional work, and control over the relationship between worker and agency) the court found that Microsoft, not the temporary agency, employed these workers.

Following plaintiffs' motion for reconsideration, the district court on October 26, 1998, issued a further "Order Regarding Motion to Revise," granting the motion in part and denying it in part. The court rejected plaintiffs' contention that it lacked authority under Rule 23 of the Federal Rules of Civil Procedure to modify the class at this stage in the litigation, citing the existence of "unusual circumstances." It went on to reject plaintiffs' contention that class membership should include all workers who ever worked in a *position* that was held by an independent contractor and then reclassified by the IRS or

contemporaneously converted by Microsoft. The court found that "[p]laintiffs are mistaken to focus on the . . . positions. A worker's position is not dispositive, and in most cases irrelevant, to the legal question presented," which the court defined as whether the worker is a common law employee of Microsoft or of a temporary agency. On that basis, plaintiffs' motion for summary judgment in favor of any employees who worked in a converted position was denied. In rejecting plaintiffs' motion, the court reaffirmed its July ruling limiting the class "to the IRS-reclassified independent contractors and any work by the same workers in the same position as converted 'temps'." The court did, however, include in the class workers who were independent contractors before becoming temps and were converted to temporary agencies voluntarily by Microsoft, i.e., who were not reclassified by the IRS but were contemporaneously converted by Microsoft.

The court acknowledged that the effect of its modification of the class, limiting membership to "a particular group of Microsoft workers, who share distinct circumstances with the named plaintiffs," was to drastically reduce it to "only a sliver of Microsoft's contingent (or non-employee) workforce." By order of December 9, 1998, the court denied plaintiffs' motion to add named plaintiffs as class representatives but allowed "workers who claim to have been misclassified common law employees of Microsoft, and to have been wrongly excluded from benefits, [to] intervene in this action." Each of those workers would, however, have to demonstrate that he or she was a common law employee of Microsoft.

Plaintiffs then moved for a permanent injunction requiring Microsoft to immediately allow all common law employees to participate in the ESPP. The district court denied the motion by order of December 22, 1998, on two grounds: (1) With respect to those workers who had been excluded from the class, plaintiffs had failed to

demonstrate "actual success on the merits," and (2) with respect to the named plaintiffs and those they represent, their legal remedies are adequate. Plaintiffs have taken an interlocutory appeal from this order, which is also pending before this panel.

Plaintiffs now petition for mandamus under the All Writs Act, 28 U.S.C. § 1651 (1994), to enforce this court's mandate in *Vizcaino* I and II. PB 15-20. They ask that the district court's orders of July 15 and October 26, 1998, reducing the plaintiff class be vacated and the original class definition reinstated. We hold that we have jurisdiction and grant the petition.

II. EXERCISE OF MANDAMUS JURISDICTION

The All Writs Act provides that "[t]he Supreme Court and all courts established by Act of Congress may issue all writs necessary or appropriate in aid of their respective jurisdictions and agreeable to the usages and principles of law." 28 U.S.C. § 1651(a) (1994). The traditional office of the writ of mandamus is to "'confine an inferior court to a lawful exercise of its prescribed jurisdiction or to compel it to exercise its authority when it is its duty to do so.'" *Will* v. *United States,* 389 U.S. 90, 95 (1967) (quoting *Roche* v. *Evaporated Milk Ass'n,* 319 U.S. 21, 26 (1943)). Thus, when a lower court obstructs the mandate of an appellate court, mandamus is the appropriate remedy. *See United States* v. *United States Dist. Ct.,* 334 U.S. 258, 263-64 (1948). The justification for mandamus in such circumstances is two-fold. First, inferior courts' disregard of appellate mandates "would severely jeopardize the supervisory role of the courts of appeals within the federal judicial system." *In re Chambers Dev. Co.,* 148 F.3d 214, 224 (3d Cir. 1998); *see also Citibank, N.A.* v. *Fullam,* 580 F.2d 82, 87 (3d Cir. 1978). Second, as a policy matter, litigants who have proceeded to judgment in higher courts "should not be

required to go through that entire process again to obtain execution of the judgment." *General Atomic Co.* v. *Felter*, 436 U.S. 493, 497 (1978).

Mandamus to compel an inferior court to follow an appellate mandate is closely related to the doctrine of law of the case. The Supreme Court long ago emphasized that when acting under an appellate court's mandate, an inferior court "is bound by the decree as the law of the case; and must carry it into execution, according to the mandate. That court cannot vary it, or examine it for any other purpose than execution." *In re Sandford Fork & Tool Co.*, 160 U.S. 247, *255* (1895); *see also Cowgill* v. *Raymark Indus., Inc.*, 832 F.2d 798, 802 (3d Cir. 1987) (law of the mandate, also called law of the case, embodies the principle that on remand "litigants should not be permitted to relitigate issues that they have already had a fair opportunity to contest"); *Firth* v. *United States*, 554 F.2d 990, 993 (9th Cir. 1977) ("When a case has been decided by an appellate court and remanded, the court to which it is remanded must proceed in accordance with the mandate and such law of the case as was established by the appellate court."). On remand, a trial court can only consider "any issue not expressly or impliedly disposed of on appeal." *Firth*, 554 F.2d at 993; *see also Nguyen* v. *United States*, 792 F.2d 1500, 1502 (9th Cir. 1986). District courts "must implement both 'the letter and the spirit of the mandate, taking into account the appellate court's opinion and the circumstances it embraces.'" *Delgrosso* v. *Spang & Co.*, 903 F.2d 234, 240 (3d Cir. 1990) (quoting *Bankers Trust Co.* v. *Bethlehem Steel Corp.*, 761 F.2d 943, 949 (3rd Cir. 1985)).

Microsoft's reliance on the so-called *Bauman* factors is misplaced. *See Bauman* v. *United States Dist. Ct.*, 557 F.2d 650, 654-55 (9th Cir. 1977). *Bauman* does not apply when mandamus is sought on the ground that the district court failed to follow the appellate court's mandate. In at least two cases decided after *Bauman*, this

court granted a writ to compel district court compliance with a prior appellate mandate without reference to *Bauman*. *See Brown* v. *Baden,* 815 F.2d 575, 576 (9th Cir. 1987) (mandamus issued to compel district court to comply with prior appellate order to reassign case); *ATSA of Cal., Inc.* v. *Continental Ins. Co.,* 754 F.2d 1394, 1396 (9th Cir. 1985) (mandamus issued to compel district court to comply with prior appellate mandate that arbitrator should determine the applicable law in commercial dispute).

Pointing out that the issuance of a writ is discretionary, *see Kerr* v. *United States Dist. Ct.,* 426 U.S. 394, 403 (1976); *Lusardi* v. *Lechner,* 855 F.2d 1062, 1070 (3d Cir. 1988), Microsoft contends that this discretion should not be exercised here because mandamus is a "drastic" remedy for "extraordinary circumstances," *Kerr,* 426 U.S. at 402-03, and not appropriate unless the right to it is "clear and indisputable." *Allied Chemical Corp.* v. *Daiflon, Inc.,* 449 U.S. 33, 35 (1980). Microsoft argues that plaintiffs cannot make that showing because the orders at issue involved class certification, a matter committed to the discretion of the district court and not now appealable. The question here, however, is whether the district court's order revising the class definition on remand conflicted with the appellate mandate. Moreover, mandamus may be appropriate even concerning traditionally discretionary matters. *See, e.g., Brown,* 815 F.2d at 576.

Microsoft's other argument, that issuance of the writ will frustrate the policy against piecemeal litigation, is inapposite. *See, e.g., Kerr,* 426 U.S. at 403; *Lusardi,* 855 F.2d at 1069; *Monti* v. *Department of Indus. Relations,* 582 F.2d 1226, 1228 (9th Cir. 1978). That policy has no relevance where mandamus is sought to compel the district court to follow the appellate mandate and avoid relitigation of final judgments. *See General Atomic,* 436 U.S. at 497 ("A litigant who . . . has obtained judgment. . .after a lengthy process of litigation . . . should

not be required to go through that entire process again to obtain execution of the judgment . . . .").

Accordingly, if the district court disregarded this court's mandate, as plaintiffs contend, mandamus is the appropriate remedy.

III. THE SCOPE OF THIS COURT'S MANDATE

The appeal before us in *Vizcaino* I and II was taken from a judgment on the merits denying relief to plaintiffs and the members of the class certified by the district court. Because that class included "[a]ll persons employed by Microsoft . . . who are denied employee benefits because they are considered independent contractors or employees of third party employment agencies, but who meet the definition of employees of Microsoft Corporation under the common law," that judgment would be res judicata with respect to the claims not only of the plaintiffs and other workers who had worked as independent contractors in positions reclassified by the IRS or voluntarily converted by Microsoft (included in the revised class) but also of all other common law employees of Microsoft (now excluded). In other words, had the judgment not been reversed, it would have been preclusive as to all the workers now excluded from the class under the district court's revised class certification. Were the case before us now in that posture—i.e., had this court affirmed rather than reversed—there is little doubt what Microsoft's position would be as to who is included in the class. Microsoft's argument that the scope of the class was not material to the issue on appeal is not tenable for that reason alone—substantial rights were at issue for all the members of the certified class.

Although the discussion in the prior opinions focused on the plaintiffs in their capacity as independent contractors rather than as temps, this was a natural

consequence of the legal posture of the case presented, not a tacit limitation on the class' claims. The class certification is a central premise of both opinions. Thus, in *Vizcaino* I, the panel relied on the Magistrate Judge's finding that "Microsoft conceded the fact that the named plaintiffs and the class they represent generally were common law employees" and that Microsoft "reserved only the right to object to the employment status of particular plaintiffs during certain periods of their tenure with Microsoft." 97 F.3d at 1193 n.4. It went on to "hold that the named plaintiffs and the class they represent are covered by the specific provisions of the ESPP." *Id.* at 1197. In *Vizcaino* II, the en banc court states that "the ESPP must, essentially, be made available to all employees" and "[t]he ESPP was created and offered to all employees." 120 F.3d at 1011, 1014. And the class is an integral element of the mandate which remanded "for the determination of any questions of individual eligibility for benefits that may remain following issuance of this opinion and for calculation of the damages or benefits due the various class members." *Vizcaino* I, 97 F.3d at 1200; *see also Vizcaino* II, 120 F.3d at 1015 ("Any remaining issues regarding the rights of a particular worker in the ESPP and his available remedies must be decided by the district court upon remand."). Thus, the district court's statement that this case is about a particular group of Microsoft employees who share "distinct circumstances" is unfounded.

Microsoft's basic contention is that the district court properly exercised its discretion to modify the scope of the class. Its brief takes a scatter-gun approach, laying down heavy fire but consisting largely of blanks.

Microsoft's major point seems to be that the certification order was only "provisional" and hence subject to alteration at a later point. Under Federal Rule of Civil Procedure 23(c)(1) a class certification order "may be conditional," but the district court's order was not

conditional, much less provisional (a concept for which Microsoft cites no authority). Over Microsoft's objection, the court "certified [the class] as plaintiffs request for all issues remaining in the case," the only qualification being that "[i]f at a later date it appears certain questions should be decertified pursuant to 23(c)(4)(A), the Court can do so." We do not interpret the statement referring to the possible withdrawal of certain issues from class treatment as a reservation of the right to substantially narrow the membership of the class at some future date. Certainly, our mandate (which runs to all common law employees of Microsoft) cannot be read as contemplating redefinition of the class; our direction to the district court to determine questions of "individual eligibility" presupposed the existence of the certified class. *Vizcaino* I, 97 F.3d at 1200. *Blake* v. *City of Los Angeles,* 595 F.2d 1367, 1385-86 (9th Cir. 1979), on which Microsoft relies, is inapposite, first, because the court of appeals did not adjudicate the merits of the claims of the individual class members and, second, because the defendant had contested the class certification and taken a cross-appeal. Microsoft chose not to contest the class certification in the district court (as the district court found, "[t]he only question is whether the class should be certified for all issues in the case, or just a few of the issues."). Had it done so and lost, it could have taken a contingent cross-appeal and, had it prevailed, the district court could have modified the class on remand.

Rule 23, moreover, does not provide authority for the modification. Rule 23(c)(1) permits a certification order to be altered or amended "before the decision on the merits," not afterward. *See Scott* v. *City of Anniston,* 682 F.2d 1353, 1357 (11th Cir. 1982) (ruling that appellate decision finding evidence sufficient to make prima facie case and insufficient to sustain proffered defense and remanding for further proceedings as to individual class members' damages was a "decision on the merits"

precluding subsequent class modification under Rule 23(c)(1)); *Jimenez* v. *Weinberger,* 523 F.2d 689, 697 (7th Cir. 1975) (holding that Rule 23(c)(1)'s "explicit permission to alter or amend a certification order before decision on the merits plainly implies disapproval of such alteration or amendment thereafter"). This court's prior decision adjudicates the merits of the plaintiff class' claim, leaving only "questions of individual eligibility for benefits that may remain . . . and calculation of the damages or benefits due the various class members." *Vizcaino* I, 97 F.3d at 1200.

Nor is there merit to Microsoft's claim that the modification was required to comply with Rule 23. In its 1993 order certifying the class under both Rules 23(b)(1)(A) and 23(b)(2), the district court found that "[p]laintiffs and defendants agree that plaintiffs' class meets the requirements of numerosity, commonality, typicality, and adequacy imposed under Fed. R. Civ. P. 23(a)." It is too late now—after a decision on the merits—to argue that commonality and typicality are lacking.

The district court's position that "unusual circumstances" permit redefinition of the class after decision on the merits lacks legal support and is erroneous. We are aware of no authorities defining what "unusual circumstances" allow a district court to circumvent the restriction imposed by Rule 23(c)(1). That the class could now comprise several thousand members rather than the "several hundred members" contemplated in the certification ruling, does not strike us as justifying a revision that wipes out the right of numerous class members to share in the benefits of the class adjudication. The "unusual circumstances" rather seem to arise from the district court's perception that the class it previously certified is "circular," i.e., that it relies on a legal conclusion to define membership in the class. According to the court, "common law employees are plaintiffs, and plaintiffs are common law employees." But the court's

reading reflects a misconception. It is implicit in the definition of the class that its members are persons who *claim* to have been (or to be) common law employees who were denied ESPP benefits. That under this definition ultimate success may turn on resolution of a disputed legal issue does not make it circular. In *Forbush* v. *J. C. Penney Co.,* 994 F.2d 1101(5th Cir. 1993), the court, dealing with an analogous situation, said:

> Penney asserts that this definition is hopelessly "circular," as the court must first determine whether an employee's pension benefits were improperly reduced before that person may be said to be a member of the class. This argument is meritless and, if accepted, would preclude certification of just about any class of persons alleging injury from a particular action. These persons are linked by this common complaint, and the possibility that some may fail to prevail on their individual claims will not defeat class membership.

Id. at 1105. Defining a class of employees as linked by their common claim to have been denied benefits to which they were entitled as common law employees is no more circular than defining a class of employees by their common claim to have been injured by their employer's unlawful actions. *See, e.g., Vaszlavik* v. *Storage Tech. Corp.,* 183 F.R.D. 264, 267 (D. Colo. 1998) (certifying plaintiffs' class defined by description of plaintiffs' legal claim).

We conclude that the district court's orders did not conform to the mandate.

IV. EXECUTION OF THE MANDATE

This court's mandate therefore left the district court no room to revise the class definition, but it charged the court with "the determination of any questions of individual eligibility for benefits." *Vizcaino* I, 97 F.3d at 1200. Plaintiffs contend that they are entitled to a class-wide judgment, encompassing not only workers in IRS-reclassified positions but also workers voluntarily converted and temps hired subsequent to conversion. Microsoft's position appears to be that, while it conceded in the district court that the named plaintiffs and the members of the class were common law employees, *see id.* at 1193 n.4, their common law employee status is now open for reexamination.

To the extent the district court granted summary judgment for plaintiffs, we agree. The named plaintiffs and others similarly situated—which to the court meant independent contractors who worked in positions reclassified by the IRS or who were voluntarily converted by Microsoft—were entitled to participate in the ESPP both before and after their conversion to temporary employees in essentially the same job positions. Microsoft's argument at this point, that its earlier concession regarding the common law employee status of the members of the class was merely arguendo, is without merit. Not only did Microsoft stand by this concession throughout the litigation but the district court also found it supported by the facts and ruled that Microsoft continued to be bound by it. We agree with the district court that this group of past and present employees is entitled to partial summary judgment, leaving for further determination only the issue of past damages. Their right to participate being clearly established, we also see no reason why those workers in this group who are currently employed by Microsoft should not now participate on an ongoing basis

in the ESPP, and entry of an order to that effect is now appropriate.

The district court further ruled, however, that its conclusion with respect to the above group could apply to temps "only insofar as their circumstances match those of the named plaintiffs (conversion to same position)." We are at a loss to understand the full import of that statement, particularly the parenthetical comment. We assume that the court meant to restrict eligibility to temps who had previously been independent contractors and had then been converted to temps in the same position. We make that assumption because the district court rejected plaintiffs' contention that workers who occupy positions reclassified as common law employees are for that reason eligible for ESPP benefits. The district court reasoned that the question presented by the temps' claim was "not whether a worker is an employee or an independent contractor . . . [but] *which* company is the worker's employer (Microsoft or the temporary agency)." The answer to that question, it said, lies in an assessment of the common law factors articulated in *Nationwide Mutual Ins. Co.* v. *Darden,* 503 U.S. 318, 323-24 (1992), although the court singled out five factors as determinative: recruitment, training, duration, right to assign additional work, and control over the relationship between worker and agency.

We agree that the assessment of the triangular relationship between worker, temporary employment agency and client is not wholly congruent with the two-party relationship involving independent contractors. In posing the question as the district court did, however, it set up a false dichotomy. Even if for some purposes a worker is considered an employee of the agency, that would not preclude his status of common law employee of Microsoft. The two are not mutually exclusive. "[In the] determination of whether a person is an employee . . . [courts look to] the usual common law factors."

Vizcaino II, 120 F.3d 1009-10 (citing *Darden,* 503 U.S. at 322). *Darden* observed that "we construe the term [employee] to incorporate 'the general common law of agency.'" 503 U.S. at 323 n.3. At common law, "a servant . . . permitted by his master to perform services for another may become the servant of such other in performing the services." Restatement (Second) of Agency § 227 (1958). "Starting with a relation of servant to one [employer], he can become the servant of another [employer] only if there are the same elements in his relation to the other as would constitute him a servant of the other were he not originally the servant of the first." *Id.* § 227 cmt. a. "Many of the factors stated in Section 220 [setting out ten traditional agency factors which are cited in *Darden,* 503 U.S. at 324] are also useful in determining whether the lent servant has become the servant of the borrowing employer." *Id.* cmt. c; *see also id.* § 226 ("A person may be the servant of two masters, not joint employers, at one time as to one act, if the service to one does not involve abandonment of the service to the other."); *Kelley* v. *Southern Pac. Co.,* 419 U.S. 318, 324 (1974) (under common law, plaintiff can establish employment by rail carrier while nominally employed by another as borrowed servant, as servant of two masters, or as subservant); *Williamson* v. *Consolidated Rail Corp.,* 926 F.2d 1344, 1348-49 (3d Cir. 1991) (following *Kelley); Nyman* v. *MacRae Bros. Constr. Co.,* 418 P.2d 253, 254 (Wash. 1966) (noting that there are three possibilities for a worker's status in a tort suit: servant of the general master; servant of the borrowing master; servant of both); *In re Earth-movers, Inc.,* 199 B.R. 62, 67 (Bankr. M.D. Fla. 1996) (finding agency and recipient of services to be "de facto 'coemployers' of [the] workers"). While this court has not heretofore addressed the specific issue, our decision in *Burrey* v. *Pacific Gas and Elec. Co.,* 159 F.3d 388 (9th Cir. 1998), is based on the premise that workers leased from an employment agency could be the common

law employees of the recipient of their services; their status with respect to the latter must be determined using the *Darden* factors. *See id.* at 394-395.

Finally, the IRS has repeatedly looked to common law principles in the determination of common law employee status in three-party employment situations. *See, e.g.,* Rev. Rul. 87-41, 1987-1 C.B. 296 (applying twenty traditional common law factors to hypothetical situations to determine whether technical service workers were employees of employment agency, without ruling whether workers were employees of client); Rev. Rul. 75-41, 1975-1 C.B. 323 (applying common law test derived from Treasury regulations to determine whether workers providing services to medical professionals pursuant to contract with a third-party professional service corporation were employees of the corporation); Rev. Rul. 66-162, 1966-1 C.B. 234 (applying Restatement (Second) of Agency § 226 (1958) in ruling that sales clerks of concessionaire in department store were employees of both concessionaire and store); 14 Standard Federal Tax Reporter (CCH) ¶ 33,538.64 at 60,589 (Jan. 28, 1999) (suggesting that traditional common law factors apply to the determination of whether technical service personnel are employees of the client they serve pursuant to a contract with a third party (e.g., employment agency)).

We conclude, therefore, that the determination of whether temps were Microsoft's common law employees turns not on whether they were also employees of an agency but rather on application of the *Darden* factors to their relationship with Microsoft. That, however, need not entangle the district court and the parties in interminable proceedings resolving the issue on a worker-by-worker basis. As the Supreme Court pointed out in *Darden,* "application [of the factors] generally turns on factual variables *within an employer's knowledge,* thus permitting categorical judgments about the 'employee' status of

claimants *with similar job descriptions*." 503 U.S. at 327 (emphasis added).

The facts of this case confirm the validity of the Court's observation in *Darden*. The IRS made its determination of employee status with reference to specific positions. In a series of letters, the IRS advised Microsoft that "we have determined that services performed for Microsoft by an individual in the position commonly referred to as [here followed the titles of various positions such as computer based training, proof reader, formatter, etc.] constitutes an employer-employee relationship . . . It is our conclusion that Microsoft either exercised, or retained the right to exercise, direction over the services performed. This control establishes an employer-employee relationship." *Vizcaino* I, 97 F.3d at 1190 n.2. The IRS determinations allow no exception for individuals in these positions on the ground that they may be on the payroll of employment agencies. Presumptively, therefore, any individual occupying an IRS reclassified position and otherwise qualified under the ESPP is an eligible common law employee—regardless of whether he or she had been personally converted from independent contractor to temp as a result of the IRS determination. The plan, by its terms, excludes short-term workers who work less than five months per year or less than half-time. There may, of course, be special circumstances affecting the rights of particular workers. The relevant facts would be within Microsoft's knowledge. The burden should therefore be on Microsoft to show why any particular worker serving in a reclassified position who meets the ESPP service requirements is not entitled to participate.

We reach the same conclusion with respect to workers in positions voluntarily converted by Microsoft. The district court found that workers who had previously been independent contractors but were voluntarily converted by Microsoft to temporary agencies contemporaneous with the IRS reclassification should also

be considered common law employees. The record does not disclose whether the voluntary conversions were of positions, in a fashion analogous to the IRS reclassification, i.e., whether Microsoft determined with reference to particular positions that services performed constitute an employer-employee relationship. If that is the case, the conclusion would be the same as in the case of the IRS reclassifications: Presumptively, any individual occupying a converted position and otherwise qualified under the ESPP is an eligible common law employee—regardless of whether he or she had been personally converted from independent contractor to temp as a result of Microsoft's conversion. If, on the other hand, Microsoft merely changed the treatment of particular individuals qua individuals, that would not inure to the benefit of other individuals hired as temps. We assume that the evidence illuminating the nature and effect of these conversions is readily available from Microsoft and will enable the district court to make the appropriate determination.

The record does not disclose whether there are in addition workers who served neither in reclassified nor converted positions but who may nevertheless be common law employees eligible to participate in the ESPP but denied benefits. The determination whether a worker was or is a Microsoft common law employee will be governed by the *Darden* factors. We leave it to the district court to determine the appropriate procedure for dealing with any such claims.

V. CONCLUSION

We held in *Vizcaino* I and II that all common law employees of Microsoft are entitled to participate in Microsoft's ESPP, subject to the exceptions specified in the plan. The members of the certified class share a common claim to past and, in certain cases, current and

future participation. They are entitled to press their claim in this action under the procedure we have outlined.

The petition is GRANTED and the matter is REMANDED to the district court for further proceedings consistent with this opinion. Because our opinion also disposes of the issues raised in plaintiffs' appeal from the denial of a permanent injunction, we DISMISS that appeal without prejudice.

UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF WASHINGTON
AT SEATTLE

DONNA VIZCAINO, et al.,	)	No. C93-178D
	)	
Plaintiffs,	)	ORDER DENYING MOTION
v.	)	TO AMEND CLASS
	)	CERTIFICATION AND
MICROSOFT, et al.,	)	GRANTING PARTIAL
	)	SUMMARY JUDGMENT
	)	
Defendants.	)	
	)	

THIS MATTER comes before the Court on plaintiffs' motion for partial summary judgment on common-law-employee status and Microsoft's motion to amend class certification. Plaintiffs move for "a ruling that they were common-law employees during all their service for Microsoft." Microsoft opposes this by arguing that the named plaintiffs are not representative of other potential class members, and therefore, the Court should certify subclasses for the question of who is a common law employee. The Court has carefully considered the briefs, declarations, and exhibits filed by the parties, and the record as a whole.[1] Microsoft's motion is denied, although the Court herein clarifies the class definition in this case. Plaintiff's motion is granted as described below.

[1] The Court finds oral argument unnecessary to decide the present motions.

I.

In 1989-90 the Internal Revenue Service (IRS) investigated the work of several classes of "freelance" workers at Microsoft and found that several hundred of them, working in nine job positions, were improperly classified as independent contractors. Microsoft retroactively classified them as employees and paid their overtime and back taxes. Then Microsoft hired a few as permanent employees, but transferred most of them to temporary employment agencies. They became "employees" of these agencies and worked at Microsoft in the positions they had previously held. The workers sought retroactive retirement benefits, health benefits, and stock options. Microsoft refused, and the workers sued.

In 1993, the Court certified a class to be represented by eight named plaintiffs, all of whom worked as independent contractors at Microsoft until the IRS re-classified them in 1990. The class was defined as follows:

> All persons employed by the Microsoft Corporation in the United States who are denied employee benefits because they are considered independent contractors or employees of third-party employment agencies, but who meet the definition of employees of Microsoft Corporation under the common law . . . .

Doc. 47 at 13. In essence, the class is defined as anyone who has worked at Microsoft who should have been a Microsoft employee but was wrongly classified otherwise. The current set of motions reveals a problem: the definition of the class—all workers who are actually common law employees—relies on a legal conclusion to identify its members. Plaintiffs' motion asks that the

Court find they are common law employees, which would amount to a finding that anyone who should be a common law employee is a common law employee (and anyone who should be a plaintiff is a plaintiff). It would not resolve anything.

While plaintiffs' arguments and evidence suggests a narrower concept of the plaintiff class—the IRS-defined group of people, pre- and post-conversion—Microsoft argues that there are many other groups of potential plaintiffs, who should not be represented by the named plaintiffs. For example, there are independent contractors whose positions were not revised by the IRS in 1989-90, and there are temporary agency employees who were never independent contractors.

Relying on these problems, Microsoft insists that the class must be divided into subclasses to determine which workers are common law employees of Microsoft. These subclasses would include (1) work done by "independent contractors" prior to the March 1990 conversion in positions the IRS found to be employee positions; and (2) work done by the same workers after their conversion to temporary employment agencies, for as long as they worked in the same positions as before conversion.[2] Microsoft proposes dividing the latter subclass into three additional subclasses based upon the different "temporary personnel agreements" (TPAs) they signed in 1990, 1991, and 1994, respectively.[3]

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[2] Curiously, none of the proposed subclasses includes any worker that was not, like the named plaintiffs, reclassified by the IRS. This despite the fact that Microsoft draws out the specter of non-reclassified independent contractors and non-converted "temps" to illustrate how different the potential plaintiffs are from the named plaintiffs.

[3] Microsoft amended the TPA each time to express more clearly and boldly the worker's waiver of any right to compensation or benefits from Microsoft.

II.

An open-ended class definition, as interpreted by the parties, is unacceptable. This case has always been about a particular group of Microsoft workers, who share distinct circumstances with the named plaintiffs. The group consists of all Microsoft workers who, like all the named plaintiffs, worked as independent contractors between 1987 and 1990 and whose positions were reclassified as employee positions after the IRS reviewed them. This case, as the Court found in its order on the scope of the remand in February, includes the claims brought by the same workers for their work after 1990, when many of them, including four named plaintiffs, were transferred to temporary employment agencies. This is the scope of the plaintiff class.

Other groups of potential claimants, those who have worked for Microsoft in a non-employee capacity, but were not reclassified by the IRS or converted by Microsoft, have never, as a practical matter, been involved in this case. At this time, they remain outside the plaintiff class.

III.

With the class definition clarified, the Court can proceed with plaintiffs' motion. Microsoft has long conceded, at the very least, that the independent contractors whom the IRS reclassified in 1990 were actually common law employees of Microsoft. Thus, plaintiffs' motion presents this question: When Microsoft transferred these workers from independent contractor status to temporary employment agencies, did those workers remain common law employees of Microsoft? Microsoft appears to concede that they did.[4] In examining the law on the matter, the Court agrees.

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[4] Inexplicably, Microsoft takes the position that only the named plaintiffs were "converted" in 1990 (and thus concedes only

The employee right at issue here, participation in Microsoft's Employee Stock Purchase Plan, arises from Internal Revenue Code § 423, which requires such programs to be available to all employees. In determining the meaning of "employee" in a statute that does not define the term, it is customary to refer to the test developed from the common law doctrine of agency. *See Nationwide Mutual Ins. Co.* v. *Darden*, 503 U.S. 318, 322-23 (1992). This "common law employee" test relies upon a non-exhaustive list of between ten and twenty factors. *Id.* at 323-24; *Hollingbery* v. *Dunn*, 68 Wn.2d 75, 80-81 (1966).

However, the question presented here is not whether a worker is an employee or an independent contractor; the question is which company is the worker's employer (Microsoft or a temporary agency). Some of the traditional factors simply cannot be used in the present analysis. For example, the location of the work, the source of the instrumentalities and tools, and the skill required in the work cannot be used to distinguish a Microsoft employee from a temporary employee. The courts that have addressed this problem appear to have simply selected applicable factors from the standard test. *See Roth v. American Hospital Supply Corp.*, 965 F.2d 862, 866-67 (10th Cir. 1992),[5] *see also* Rev. Rul. 87-41, 1987-1 C.B. 296.

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that the named plaintiffs remained common law employees after conversion). Def. Opp. (#376) at 3.14. This is clearly belied by Microsoft records, which show scores, if not hundreds, of employees that went from independent contracts to temporary agencies in early 1990. Bernard Dec. (#377), Ex. E. The IRS admittedly reclassified some 7-9 job categories as employee positions in late 1989; anyone who held one of these positions at the time and became a "temp" without changing jobs is obviously in the same situation as the named plaintiffs.

[5] *Professional & Executive Leasing, Inc.* v. *Commissioner*, 862 F.2d 751, 753 (9th Cir. 1988), analyzed whether certain professional workers were employees of a temporary agency, but did not compare the workers' relationships with two different

Plaintiffs ignore this problem and argue that the most important factor in the test is the degree of control the hiring company has over the worker.[6] Employer control is not always an appropriate basis for distinguishing a temporary and a regular employee. Traditionally, bona fide temporary workers work at client companies either for a specific project or for a limited time. In the project-based assignment, the client's authority to assign tasks outside or beyond the project would indicate an employer relationship, but daily supervision within the project would not. In the time-limited assignment, client control of the worker would be expected to the same degree as with comparable employees of the client.

In the Court's judgment, the factors to consider in determining whether a "temporary employee" is a common law employee of the client company include (1) whether the client or the agency recruited the worker, (2) the extent of the training that the client provides to the worker, (3) the duration of the worker's relationship with the client company, (4) the client company's right to assign additional projects to the worker, and (5) whether

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employers. *See also* Rev. Rul. 75-41, 1975-2 C.B. 323. *Daughtrey* v. *Honeywell, Inc.*, 3 F.3d 1488, 1492-93 (11th Cir. 1993) addressed a claim to employee benefits by a worker who was classified both as an independent contractor and as an agency employee, but the court did not analyze the difference.

[6] On its own motion to amend the class certification, Microsoft argues IRS regulations provide a distinct standard in their definition of "employer." *See* 26 C.F.R. 31.3401(d)-1. It suggests that whoever controls the payment of wages is the employer. However, cases interpreting this have held that it does not mean the common law employer can simply contract away its obligations to an employee leasing company. *See, e.g., In re Earthmovers, Inc.*, 199 B.R. 62, 66-67 (Bankr. M.D. Fla. 1996). The argument is also inconsistent with another Microsoft makes, that transfer from the client's payroll to the temporary agency's payroll is the key factor.

the client company may influence the relationship between the worker and the agency. As with the distinction between an independent contractor and an employee, "all of the incidents of the relationship must be assessed and weighed with no one factor being decisive." *Darden*, 503 U.S. at 324 (quoting *NLRB* v. *United Ins. Co. of America*, 390 U.S. 254, 258 (1968)).

Of the eight named plaintiffs, five worked for Microsoft not only as independent contractors but later as temporary agency employees. Four of these plaintiffs (Mark Stout, Thomas Morgan, and Elizabeth and Larry Spokoiny) were "converted" from one status to the other in around March 1990.[7] All of them claim they had no contact with their respective temporary agencies except to receive paychecks and W-2 forms. All of them claim to have signed agreements with or involving a temporary agency at Microsoft's command, at Microsoft's workplace. (One, Thomas Morgan, nominally worked for three temporary agencies at one time, but performed all his work for Microsoft.) They claim to have worked on various projects both before and after "conversion," and their work relationship with Microsoft appears to have been indefinite. On the evidence submitted, there is no genuine issue of material fact that these four plaintiffs were common law employees of Microsoft during their work there as "temporary personnel." The Court therefore grants partial summary judgment to plaintiffs that they were common law employees of Microsoft, both before and after conversion.

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[7] The fifth, Jon Waite, was terminated as an independent contractor prior to conversion and rehired as temporary personnel after conversion. Therefore, he was not "converted," although he was recruited directly by Microsoft. On the evidence submitted, he presents several indicia of being a Microsoft employee. For the time being, however, the Court declines to determine whether he was a common law employee of Microsoft when he worked for temporary employment agencies.

IV.

In sum, the Court finds that the class definition needs clarification to include only the named plaintiffs and those similarly situated, both before and after conversion to temporary employment. As such, they have shown they were common law employees of Microsoft during both periods of employment.

THEREFORE, defendant's motion to amend class certification is DENIED, and plaintiffs' motion for partial summary judgment is GRANTED.

The Clerk of the Court is directed to send copies of this order to all counsel of record.

DATED this 15th day of July, 1998.

s/
Carolyn R. Dimmick
United States District Judge

UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF WASHINGTON
AT SEATTLE

DONNA VIZCAINO, et al.,	)	No. C93-178 D
	)	
Plaintiffs,	)	ORDER REGARDING
	)	MOTION TO REVISE
v.	)	
	)	
MICROSOFT, et al.,	)	
	)	
Defendants.	)	

THIS MATTER comes before the Court on plaintiffs' motion for a revision or clarification of the Court's order of July 15, 1998 and for partial summary judgment accordingly. The Court grants the motion insofar as it clarifies the issues disputed and finds all "converted" workers are members of the plaintiff class.[1] The remainder of the motion is denied.

Plaintiffs' motion is a motion for reconsideration, yet does not follow the rules for such a motion, Local Rule CR 7(e). As such, it could, and for many reason should, be summarily denied. However, both parties have displayed a penchant for re-arguing issues already decided by this Court, indicating a great need for clarification. Moreover, one group of workers who could potentially participate in this case has been identified and addressed for the first

[1] As discussed in section II.C. below, this includes not only the independent contractors Microsoft converted to temporary agency employees because the Internal Revenue Service (IRS) found their positions were improperly classified, but also those workers whom Microsoft voluntarily converted.

time on this motion, and the Court finds they belong in the plaintiff class.

I.

This case was originally brought in 1993 by contingent workers at defendant Microsoft Corporation, people who had served at Microsoft as independent contractors or temporary employees or both, to recover employee benefits denied to them because they were not "regular" employees. It began with a 1989 investigation by the IRS of several job positions that Microsoft was filling with independent contractors, referred to by Microsoft as "freelance workers." The IRS determined that workers in some positions should be Microsoft employees for federal tax purposes. Shortly thereafter, Microsoft began "converting" these workers. To some it offered permanent employee positions, but most had to sign up with one of several temporary employment agencies or leave Microsoft altogether. Microsoft apparently converted not only those independent contractors whose positions were reclassified by the IRS, but also many other independent contractors.

Some workers demanded employee benefits. Microsoft refused, and eight of them filed this suit. On July 21, 1993, the Court certified a class of plaintiffs defined as

> All persons employed by Microsoft Corporation in the United States who are denied employee benefits because they are considered independent contractors or employees of third-party employment agencies but who meet the definition of employees of Microsoft Corporation under the common law. This definition includes

> all such persons so employed within the applicable statute of limitations.

Doc. 47 at 13. This definition is the source of today's problems.

In early 1994, United States Magistrate Judge David E. Wilson heard cross-motions for summary judgment in this case regarding each of several Microsoft employee benefits. In April 1994, Judge Wilson recommended granting partial summary judgment in favor of Microsoft and partial summary judgment in favor of plaintiffs. Regarding plaintiffs' claims for benefits under state law, Judge Wilson found plaintiffs had no contractual right to any of them except one, the Employee Stock Purchase Plan (ESPP), because that plan evinces an intent to comply with Internal Revenue Code (IRC) § 423, which requires that it be available to all employees. Doc. No. 187 at 25-26, 34. Microsoft did not argue plaintiffs were not its common law employees. *Id.* at 34.

Regarding plaintiffs' claims to benefits governed by the Employee Retirement Income Security Act (ERISA), Judge Wilson would have rejected plaintiffs' claims to health and life insurance benefits, but granted their claims to Microsoft's Savings Plus Plan (SPP), a retirement program under IRC § 401(k). Doc. No. 191 at 9, 12-13. He found that while the other plans employed clear restrictions upon eligibility, the SPP did not, and should be available to all of Microsoft's common law employees. *See id.* at 13-14. Again, Microsoft did not contend the plaintiffs were not its employees.

This Court adopted Judge Wilson's recommendations only insofar as they favored Microsoft. As to the ESPP, the Court found that defendant's intent to comply with IRC § 423 did not give plaintiffs a personal right to participate in the plan, and the Court found a clear restriction in the SPP that excluded plaintiffs. *See* Doc. Nos. 223 & 225. The Court found that plaintiffs'

contractual agreements excluding them from employee benefits precluded their claims, regardless of their employee status.

Plaintiffs appealed the Court's conclusions regarding the ESPP and the SPP, and the Ninth Circuit reversed. First, it held that since defendant conceded plaintiffs' status as common law employees, the Plan Administrator's decision that they were ineligible for SPP benefits was wrong.[2] *Vizcaino* v. *Microsoft Corp.*, 120 F.3d 1006, 1013 (9th Cir. 1997). Second, it held that the plaintiffs' written agreements with defendant, which stated that they would not receive employee benefits, was mistaken and therefore did not have the effect of depriving plaintiffs of ESPP participation, *id.* at 1012, and that defendant's offer of ESPP participation was made to all employees, including plaintiffs, who accepted it by virtue of their labor. *Id.* at 1014-15. The court remanded the remaining issues under the ESPP to this Court, and under the SPP to the Plan Administrator.

Since that time, the parties have vigorously disputed two issues: who is in the class of plaintiffs and how much should they recover. This motion relates to who is in the plaintiff class. In February 1998, the Court denied Microsoft's motion to limit the class and its claims to the benefits plaintiffs lost as independent contractors, before conversion to temporary agencies. Doc. No. 307. The Court held, however, that Microsoft could challenge the right of temporary agency employees to participate in

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[2] The SPP's terms require it be offered to employees on Microsoft's United States payroll. Judge Wilson found this ambiguous and construed it against Microsoft. Doc. No. 191 at 20. This Court found the language clearly excludes plaintiffs, who were not paid through the payroll department. Doc. No. 225 at 3. The Ninth Circuit found that since the Plan Administrator did not consider this language, the question should be remanded to the Plan Administrator for that purpose. *Vizcaino* v. *Microsoft Corp.*, 120 F.3d 1006, 1013 (9th Cir. 1997).

the ESPP by demonstrating that they were not its common law employees. *See id.* at 8. In other words, the Court in February limited Microsoft's concession about plaintiffs' status to the people who worked as independent contractors, *when* they worked as independent contractors.

In July 1998, the Court granted plaintiffs' motion for an order finding they were common law employees of Microsoft during all of their service for the company. First, however, it had to better define who plaintiffs were, and who they were not. It had become increasingly clear that the named plaintiffs, all of who had, like several hundred others, worked as independent contractors and been reclassified by the IRS (and most of whom had then become temps), represented only a sliver of Microsoft's contingent workforce.

The Court decided that the named plaintiffs could represent only those who shared with them the unique circumstances they had presented throughout this case: They had been reclassified in 1989 by the IRS. Microsoft's concession (and the IRS investigation, though not binding on the Court) had established that these people were its employees. Since plaintiffs had demonstrated that they remained common law employees of Microsoft after being "converted" to temporary agencies, the class could claim lost benefits both before and after conversion.

Plaintiffs now move to have the Court "revise or clarify" this order to allow several groups of excluded workers to participate in this case, and for summary judgment that the Court's findings to date apply to those workers.

II.

A.

The July 15, 1998 order attempted to resolve the problems inherent in the original class definition. By purporting to include all misclassified common law employees of Microsoft, the definition relies upon a legal conclusion to identify its members. When the parties avoided addressing that legal issue by stipulation, they created a circular class mechanism: Common law employees are plaintiffs, and plaintiffs are common law employees.[3]

Plaintiffs refuse to recognize this problem.[4] They claim that since the contingent fact, whether one is a common law employee of Microsoft, is discernable by reference to objective standards, there is no circularity problem. This ignores the issue at hand—identifying the members of the class. If one wanted award stock to all

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[3] Clearly, the Court understood the proposed class to consist only of the freelance workers that the IRS determined were Microsoft employees in 1989. *See id.* at 11 ("There are clearly common issues for *all potential class members* .... The Internal Revenue Service has already made a determination that *they* are common law employees for tax purposes." (emphasis added)). It said the class "could have up to several hundred members." Doc. No. 47 at 10. (This was plaintiffs' estimate of the size of the class as well, see Doc. No. 8 at 5.) The number of contingent workers at Microsoft, which plaintiffs now seek to include in the class, is probably *currently* over 5,000.

[4] Plaintiffs' arguments that the Court cannot redefine the class at this stage are trumped by the practical need to do so (which the Court already ruled), and are not persuasive. *See, e.g., Scott* v. *City of Anniston,* 682 F.2d 1353, 1357 (11th Cir. 1982) (Federal Rule of Civil Procedure 23(c)(1) "does not appear to permit a court, *absent unusual circumstances,* to amend the class after a decision on the merits" (emphasis added). Plaintiffs ignore and omit the highlighted clause, which could not be more aptly invoked than in this case.).

Microsoft employees with type O negative blood, one would have an objective criterion, and yet would not know *which* employees had O negative blood. (The ones in the set. Which ones are in the set? The ones with O negative blood.)

Nor can Microsoft's concession that "plaintiffs" are generally common law employees of the company serve as the anchor in defining the class. The concession is merely a truism. Of course plaintiffs are common law employees of Microsoft. That is what the definition itself says. Plaintiffs claim that anyone who is a misclassified common law employee of Microsoft is a plaintiff, and anyone who is a plaintiff is a misclassified common law employee of Microsoft. This is not a tenable approach to resolving this case.

B.

Plaintiffs actually argue that the class *potentially* includes every contingent worker who ever (within the statute of limitations) worked at Microsoft. They argue that a very large group of these workers have already been found to be common law employees of Microsoft, and are thus class members. And they propose that the Court "establish a procedure" for identifying all of the other misclassified contingent workers since 1987.

According to plaintiffs, the class should presently include all workers who ever worked in a *position* at Microsoft that was ever held by an independent contractor and then reclassified by the IRS or Microsoft to an employee position. Most of these have been excluded by the Court's July 15 order. Plaintiffs identify these excluded workers as belonging to one of several discrete groups.[5] They do not argue that any of these discrete

[5] These include: (1) IRS-reclassified workers who were not converted; (2) workers converted from "freelancer" to "temp" voluntarily by Microsoft; (3) workers who had been in IRS-

groups are entitled to be called common law employees of Microsoft because of the nature of their relationship with Microsoft. Instead, they argue that this has already been established by the prior litigation of this case, including the Ninth Circuit's mandate on remand. They say "no material distinction exists" between the named plaintiffs and these others. Apparently, this is based upon their having held a position once reclassified by the IRS or Microsoft.

Plaintiffs are mistaken to focus on the reclassified *positions*. A worker's position is not dispositive, and is in most cases irrelevant, to the legal question presented. Almost of all of the work these excluded workers did, they did as "temps" (the exception is discussed below). The Court's July order held that whether a temp is a common law employee of the client is a different question than whether an independent contractor is an employee of the hiring party. The IRS determination about independent contractors is not dispositive as to temps. *Any* position at Microsoft could lawfully be filled by a temporary agency employee if the employee's relationship with Microsoft were *temporary*. Therefore, the excluded workers should not automatically be class members (and considered common law employees of Microsoft) because of their positions.

Ironically, plaintiffs' position recognizes a fact they overtly resist: Some attribute of the named plaintiffs must have implied a limitation upon the original class definition. Plaintiffs contend that anyone related by position to the named plaintiffs (or to voluntarily converted workers) should be a member of the class and held to have been a common law employee of Microsoft. But this position-limitation appears nowhere in the original class definition. It comes from the way this case has been litigated. Until

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reclassified positions, left Microsoft and returned as temps; and (4) temps hired after conversion.

remand, the courts and the parties had focused their analyses almost exclusively upon the 1987-90 independent contractors whose positions were reclassified by the IRS. That is why this Court, in July, ordered the class limited to those workers. Plaintiffs prefer that it be limited to those *positions*. Thus, while they say any modification is wrong, what they really want is simply a more favorable modification.

The Court's modification—that the class represented by the named plaintiffs is limited to the IRS-reclassified independent contractors and any work by the same workers in the same positions but as converted "temps"—is based upon the facts that characterized the named plaintiffs' relationship with Microsoft.[6] Clearly, the named plaintiffs have established their status as common law employees during the 1987-90 period, by virtue of Microsoft's admission.[7] *See, e.g.*, 2/13/98 Order at 7. This Court further found that these same workers remained common law employees of Microsoft after they were converted to temporary employees. 7/15/98 Order at 8. The Court did this by finding an appropriate set of factors

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[6] This relationship corresponds with the "common law employee" limitation in the original class definition.

[7] This should clarify one apparent point of uncertainty with plaintiffs, that certain workers who never became temps (e.g. Donna Vizcaino) are members and entitled to summary judgment regarding their status. *See* Plfs' Brief (Doc. No. 441) at 5 & n. 13.

Plaintiffs present new information regarding named plaintiff Thomas Morgan, that he was converted in 1988 (although his original declaration indicates he was converted in 1989). Morgan's claims as a freelancer is established, since his position was reclassified by the IRS. The Court specifically found that his work as a temp was similarly mislabeled. 7/15/98 Order at 7-8. It appears he is entitled to that ruling whether he was converted in 1988 or 1989.

and applying them to the named plaintiffs.[8] The reason this holding (and the class itself) was limited to these *workers* in these *positions* is because those two factors help to establish the workers' post-conversion status. We know, for example, that named plaintiff Mark Stout was a common law employee of Microsoft in February 1990, working as a production editor, when he became a temporary agency employee, working as a production editor. It is clear from this alone (and Microsoft's acquiescence) that there was no temporal limitation (explicit or otherwise) upon Stout's post-conversion work at Microsoft, that Microsoft "recruited" Stout, and that Stout's relationship with his agency employer was created by Microsoft. These facts, in the Court's analysis, established that Stout was a common law employee of Microsoft during his work as a temp from February 1990 to March 1991. *See* Stout Dec. (Doc. No. 14), & Exh. 1. Had Stout switched positions upon conversion, or left Microsoft prior to conversion and then returned later, it would not be so clear that he did not become a short-term project employee, *i.e.*, a bona fide temp.[9]

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[8] Those factors include:

> (1) whether the client or the agency recruited the worker, (2) the extent of the training that the client provides to the worker, (3) the duration of the worker's relationship with the client company, (4) the client company's right to assign additional projects to the worker, and (5) whether the client company may influence the relationship between the worker and the agency.

10/15/98 Order at 7.

[9] One named plaintiff, Jon Waite, did leave his IRS-reclassified position prior to conversion, and returned later to another such position as a temp. When the Court held that the named plaintiffs were Microsoft employees during their post-conversion work as temps, it withheld a decision as to Waite's post-

To put this another way, the legal conclusions the courts have reached regarding the named plaintiffs can be assumed to apply to Microsoft's "temps" only insofar as their circumstances match those of the named plaintiffs (conversion to same position), just as the Court ordered. The Court will not apply those conclusions to other temps, whose circumstances may vary wildly, from each other and from the named plaintiffs.

C.

There is one group of workers plaintiffs claim have been improperly excluded from this action which consists of workers who were independent contractors before becoming temps. These are the workers who were independent contractors at Microsoft between 1987-90 and who were thereafter "converted" to temporary agencies *voluntarily* by Microsoft. That is the IRS did not reclassify these workers,[10] but Microsoft saw fit to change their formal status along with the reclassified workers.

Plaintiffs contend there is no material difference these "voluntary converts" and the named plaintiffs, suggesting that Microsoft conducted its own investigation of freelancers and found these additional workers were also misclassified. They say the voluntary conversion, moreover, is an "admission" that the workers were company employees. Microsoft claims no investigation

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conversion work, because of the uncertainty described here. Both sides have filed motions for summary judgment on this point.

[10] Again, plaintiffs refer to many *positions*, not workers, that Microsoft converted voluntarily. This emphasis is wrong because, as independent contractors, they have rights to benefits, if at all, by virtue of the conversion and admission, and as temps, by demonstrating that their relationship with Microsoft was not "temporary." Both of these sources depend upon individual worker circumstances, not positions. In this discussion, the Court considers *workers* converted in early 1990 only.

took place, and it merely instituted a policy that all independent contractors had to submit an IRS-approved SS-8 form (qualifying them as independent contractors), or they would be reclassified as temps, or perhaps in some cases regular employees. Microsoft also claims that some of the freelancer positions it converted voluntarily were actually approved by the IRS as independent contractor positions.[11]

The Court finds there is good reason to include the voluntary converts in the class as presently represented. First is Microsoft's admissions *in this litigation* that "plaintiffs" are its common law employees (which it did throughout dismissal and appeal, see 2/13/98 Order at 6-7). Although the Court has said that Microsoft's concession in this case should not mean that it admits all its contingent workers were and are misclassified common law employees of the company, the concession should be limited only as reasonably necessary. Unlike the other excluded workers, there is an important identity between the named plaintiffs and the voluntary converts. At the point when Microsoft's freelance practices were under attack by the IRS, it converted these workers. Thus, the voluntary converts appears in the narrative of this case.

Second, just as there is actual evidence that the workers reclassified by the IRS were common law employees (the IRS's analysis), the same can be said of the voluntary converts. This is because it is most unlikely that a bona fide independent contractor *could* be

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[11] In support of this it cites evidence of people/positions converted, but not of whether they were found to be independent contractors. The only evidence the Court finds is a letter from the IRS agent saying "We agreed that for 1986 and 1987 we would treat" certain positions as independent contractors. Stobaugh Dec. (Doc. No. 444) Ex. B at 004291. This does not mean the IRS found they were *properly* independent contractors in *1989-90*.

converted to a temporary employee. An independent contractor usually exhibits some of the following attributes: exerts control over details of his work; is engaged in a distinct line of work; receives little supervision; supplies his own tools; is paid by the job; and performs work outside the regular business of the employer. *See Hollingberry* v. *Dunn*, 68 Wn.2d 75, 80-81 (1966). A temporary worker is an employee of a third-party agency, and we know that in the case of the voluntary converts, those agencies were selected by Microsoft. A temporary worker may be recruited or trained by his agency, and may work for several clients, on assignment by the agency. Each assignment will be limited in duration or scope, and the worker's relationship with the agency should exist independent of his relationship with a client. *See* 7/15/98 Order at 7. It hardly seems possible that a bona fide independent contractor could be converted by the "client" into a bona fide temporary agency employee.

While these reasons are not sufficient to compel the conclusion that the 1990 voluntary converts were common law employees of Microsoft, they support a presumption in their favor. Microsoft has failed to demonstrate that any of these workers was not its common law employee, and therefore the Court so finds.

On the present record, the Court finds that those workers who served Microsoft as independent contractors or "freelancers" between 1987 and 1990 *and* were voluntarily converted to temporary employees by Microsoft in 1989-90 are members of the class represented by named plaintiffs, and entitled to the benefits of all judgments rendered in plaintiffs' favor.

D.

Finally, plaintiffs also describe a fifth "excluded" group of workers, the "all others" category. Plaintiffs

provide no basis upon which to conclude that this completely amorphous group belongs in the plaintiff class.

III.

THEREFORE, plaintiffs' motion to revise or clarify the Court's July 15, 1998 order IS DENIED IN PART and GRANTED IN PART.

The Clerk of the Court is directed to send copies of this order to all counsel of record.

DATED this 26th day of October, 1998.

s/_____
Carolyn R. Dimmick
United States District Judge

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

DONNA VIZCAINO; JON R. WAITE; MARK STOUT; GEOFFREY CULBERT; LESLEY STUART; THOMAS MORGAN; ELIZABETH SPOKOINY; LARRY SPOKOINY,	)	No. 94-35770
Plaintiffs-Appellants,	)	D.C. No. CV-93-00178-CRD
v.	)	OPINION
MICROSOFT CORPORATION, and its pension and welfare benefit plans, et al.,	)	
Defendants-Appellees.	)	

Appeal from the United States District Court
for the Western District of Washington
Carolyn R. Dimmick, District Judge, Presiding

Argued and Submitted
March 27, 1997

Decided July 24, 1997

Before: HUG, Chief Judge, and Browning, Fletcher, Pregerson, Hall, O'Scannlain, Fernandez, T.G. Nelson, Hawkins, Tashima, and Thomas, Circuit Judges

Opinion by Judge Fernandez; Partial Concurrence and Partial Dissent by Judge Fletcher; Partial Concurrence and Partial Dissent by Judge O'Scannlain

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Linda J. Dunn, Office of the Attorney General, Seattle, WA, for amicus Washington State Department of Labor and Industries.

OPINION

FERNANDEZ, Circuit Judge.

Donna Vizcaino, Jon R. Waite, Mark Stout, Geoffrey Culbert, Lesley Stuart, Thomas Morgan, Elizabeth Spokoiny, and Larry Spokoiny brought this action on behalf of

themselves and a court-certified class (all are hereafter collectively referred to as "the Workers"). They sued Microsoft Corporation and its various pension and welfare plans, including its Savings Plus Plan (SPP), and sought a determination that they were entitled to participate in the plan benefits because those benefits were available to Microsoft's common law employees. The district court granted summary judgment against the Workers, and they appealed the determinations that they were not entitled to participate in the SPP or in the Employee Stock Purchase Plan (ESPP). We reversed the district court because we decided that the Workers were common law employees who were not properly excluded from participation in those plans. *See Vizcaino v. Microsoft Corp.*, 97 F.3d 1187 (9th Cir.1996) (*Vizcaino I*). However, we then decided to rehear the matter en banc, and we now agree with much of the panel's conclusion and reverse the district court.

BACKGROUND

At various times before 1990, Microsoft hired the Workers to perform services for it. They did perform those services over a continuous period, often exceeding two years. They were hired to work on specific projects and performed a number of different functions, such as production editing, proofreading, formatting, indexing, and testing. "Microsoft fully integrated [the Workers] into its workforce: they often worked on teams along with regular employees, sharing the same supervisors, performing identical functions, and working the same core hours. Because Microsoft required that they work on site, they received admittance card keys, office equipment and supplies from the company." *Id.* at 1190. However, they were not paid for their services through the payroll department,

but rather submitted invoices to and were paid through the accounts payable department.

Microsoft did not withhold income or Federal Insurance Contribution Act taxes from the Workers' wages, and did not pay the employer's share of the FICA taxes. Moreover, Microsoft did not allow the Workers to participate in the SPP or the ESPP. The Workers did not complain about those arrangements at that time.

However, in 1989 and 1990 the Internal Revenue Service examined Microsoft's records and decided that it should have been withholding and paying over taxes because, as a matter of law, the Workers were employees rather than independent contractors. It made that determination by applying common law principles. Microsoft agreed with the IRS and made the necessary corrections for the past by issuing W-2 forms to the Workers and by paying the employer's share of FICA taxes to the government.

Microsoft also realized that, because the Workers were employees, at least for tax purposes, it had to change its system. It made no sense to have employees paid through the accounts payable department, so those who remained in essentially the same relationship as before were tendered offers to become acknowledged employees. Others had to discontinue working for Microsoft, but did have the opportunity to go to work for a temporary employment agency, which could then supply temporary Workers to Microsoft on an as-needed basis. Some took advantage of that opportunity, some—like Vizcaino—did not.

The Workers then asserted that they were employees of Microsoft and should have had the opportunity of

participating in the SPP and the ESPP because those plans were available to all employees who met certain other participation qualifications, which are not relevant to the issues before us. Microsoft disagreed, and the Workers asked the SPP plan administrator to exercise his authority to declare that they were eligible for the benefits. A panel was convened; it ruled that the Workers were not entitled to any benefits from ERISA plans[1] —for example, the SPP—or, for that matter, from non-ERISA plans—for example, the ESPP. That, the administrative panel seemed to say, was because the Workers had agreed that they were independent contractors and because they had waived the right to participate in benefit plans. This action followed.

JURISDICTION AND STANDARD OF REVIEW

The district court had jurisdiction pursuant to 29 U.S.C. § 1132(e)(1) and 28 U.S.C. §§ 1331 and 1367(a). We have jurisdiction pursuant to 28 U.S.C. § 1291.

We review the district court's grant of summary judgment de novo. *See Bagdadi v. Nazar*, 84 F.3d 1194, 1197 (9th Cir.1996). However, when reviewing the decision of a plan administrator who has discretion, "the exercise of that discretion is reviewed under the arbitrary or capricious standard, or for abuse of discretion, which comes to the same thing." *Snow v. Standard Ins. Co.*, 87 F.3d 327, 330 (9th Cir.1996); *see also Saffle v. Sierra Pac. Power Co. Bargaining Unit Long Term Disability Income Plan*, 85 F.3d 455, 458 (9th Cir.1996).

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[1] *See* Employee Retirement Income Security Act of 1974, Pub. L. No. 93-406, 88 Stat. 829 (1974).

DISCUSSION

Although the Workers challenge both their exclusion from the SPP and their exclusion from the ESPP, the two plans are subject to rather different legal regimes. The former is a 26 U.S.C. § 401(k) plan, which is governed by ERISA; the latter is a 26 U.S.C. § 423 plan, which is not governed by ERISA. It, instead, is governed, at least in large part, by principles arising out of the law of the State of Washington. Nevertheless, certain issues, perhaps the most critical ones, cut across both regimes, and we will address them first.

I. GENERAL CONSIDERATIONS.

A. The Workers' Status.

It is important to recognize that there is no longer any question that the Workers were employees of Microsoft, and not independent contractors. The IRS clearly determined that they were. In theory one could argue that what the IRS said was fine for withholding and FICA purposes, but that is as far as it goes.

However, the IRS made its determination based upon the list of factors which is generally used to decide whether a person is an independent contractor or an employee. *See* 26 C.F.R. § 31.340(c)-1(b). The same essential definition is used for § 401(k) plans, *see* 26 C.F.R. § 1.4010(b)-9, and for § 423 plans, *see* 26 C.F.R. §§ 1.423-2(e)(2), 1.421-7(h). That there should be a congruence of approaches is not surprising. As the Supreme Court has pointed out, when Congress uses the work "employee," courts "'must infer, unless the statute otherwise dictates, that Congress means

to incorporate the established meaning'" of that word. *Nationwide Mut. Ins. Co. v. Darden*, 503 U.S. 318, 322, 112 S.Ct. 1344, 1348, 117 L.Ed.2d 581 (1992). The Court then went on to scrutinize the various typical factors that go into a determination of whether a person is an employee. *See id.* at 323-24, 112 S.Ct. at 1348. Those were the usual common law factors. But, again, we recognize that one could still question the IRS's application of those factors in a particular case.

That question is obviated here for, perhaps more to the purpose, both Microsoft and the SPP have conceded for purposes of this appeal that the Workers were common law employees. In fact, they have asserted that the Workers' status is a "nonissue" because they concede that the Workers were common law employees. That is to say, they were employees of Microsoft.

B. The Employment Agreements.

The concession that the Workers were employees would, at first blush, appear to dispose of this case. It means that for legal purposes they, along with the other employees of Microsoft, were subject to Microsoft's control as to both "the manner and means" of accomplishing their job, that they worked for a substantial period, that they were furnished a workplace and equipment, that they were subject to discharge, and the like. *See id.*; *see also* 26 C.F.R. § 31.3401(c)-1(b). If that were all, this would be an exceedingly easy case. Of course, it is not all.

Microsoft also entered into special agreements with the Workers, and it is those which complicate matters to some extent. Each of the Workers and Microsoft signed

agreements which stated, among other things not relevant here, that the worker was "an Independent Contractor for [Microsoft]," and nothing in the agreement should be construed as creating an "employer-employee relationship." As a result, the worker agreed "to be responsible for all of [his] federal and state taxes, withholding, social security, insurance, and other benefits." At the same time, Microsoft had the Workers sign an information form, which explained: "[A]s an Independent Contractor to Microsoft, you are self employed and are responsible to pay all your own insurance and benefits. . . Microsoft . . . will not subject your payments to any withholding. . . . You are not either an employee of Microsoft, or a temporary employee of Microsoft." We now know beyond peradventure that most of this was not, in fact, true because the Workers actually were employees rather than independent contractors. What are we to make of that?

We now know that as a matter of law Microsoft hired the Workers to perform their services as employees and that the Workers performed those services. Yet we are also obligated to construe the agreements. *See Republic of Nicaragua v. Standard Fruit Co.*, 937 F.2d 469, 474 (9th Cir.1991); *Swanson v. Liquid Air Corp.*, 118 Wash.2d 512, 521, 826 P.2d 664, 669 (1992). In doing so, we could take either a negative or a positive view of Microsoft's intent and motives. We could decide that Microsoft knew that the Workers were employees, but chose to paste the independent contractor label upon them after making a rather amazing series of decisions to violate the law. Or we could decide that Microsoft mistakenly thought that the Workers were independent contractors and that all else simply seemed to flow from that status.

Were we to take the former approach, we would have to determine that Microsoft, with the knowledge that the Workers were simply a group of employees, decided to engage in the following maneuvers:

(1) Despite the requirements of federal law that amounts be withheld from employee wages, Microsoft decided it would not withhold. *See* 26 U.S.C.§§ 3102, 3401-3406.

(2) Despite the fact that the SPP states that "employee" means "any common law employee . . . who is on the United States payroll of the employer," Microsoft decided to manipulate the availability of that benefit by routing the wages of these employees through the accounts payable department, so that it could argue that they were not on the United States payroll. Beyond that, it also determined that it would tell the IRS in its "Application for Determination for Defined Contribution Plan," that Microsoft did, indeed, basically include all employees, a category that it knew included the Workers, even thought it had contrived to exclude them. Beyond even that, Microsoft excluded these employees when it filed its tax returns for the SPP, even though it knew better.

(3) Despite the fact that the ESPP must, essentially, be made available to all employees, Microsoft excluded these employees and thereby intentionally risked the possibility that the plan would not qualify for favorable tax treatment. It did that, even though the plan itself stated that it covered all regular employees and that it was to be construed to comply with 26 U.S.C. § 423, a law which basically requires that all employees be covered. The officers of Microsoft also decided to eliminate one group of common law employees

from the benefits, even though the board of directors and the shareholders had already made the benefits of the ESPP available to those employees. In doing that, the officers intentionally violated the corporate law of Delaware, to which Microsoft was subject, because the terms of coverage of stock option plans are not in the hands of corporate officers; they are in the hands of the board itself. *See Del. Code Ann. tit.* 8 § 157; *see also Michelson v. Duncan*, 386 A.2d 1144, 1150-51 (Del.Ch.1978), *aff'd in part and rev'd in part on other grounds*, 407 A.2d 211 (Del.1979).

On the other hand, in construing the agreements we can view the label as a simple mistake. That is, Microsoft honestly thought that the Workers were independent contractors and took its various actions and inactions based upon that misapprehension. Its actions and the conclusions conveyed to the Workers in the agreements and in the explanation in the information form, which accompanied the agreements, were simply an explication of what the effect of independent contractor status would be and had no separate purpose or effect aside from that explanatory function. That is to say, of course there could neither be withholding from wages nor participation in the benefit plans because those keyed on common law employment status. If the Workers were independent contractors, those would be the inevitable results, even if nothing were said about them in the agreement or the information form. Explaining the meaning of independent contractor status was simply a helpful disclosure.

Absent evidence that the officers of Microsoft used their daedalian talents to follow the first route we have just outlined, we must decide that the second route is a more accurate portrayal of what occurred here. In other words,

we should, and we do, consider what the parties did in the best light. In so doing, we do not believe that we are being panglossian; we are merely acting in accordance with the ancient maxim which assumes that "the law has been obeyed." *See, e.g.*, Cal. Civ.Code § 3548.

The evidence does not undercut our approach; it supports it. As soon as Microsoft realized that the IRS, at least, thought that the Workers were employees, it took steps to correct its error. It put some of them on its United States payroll forthwith. It also gave the Workers retroactive pay for overtime hours. If Microsoft had been withholding taxes while failing to provide benefits, that would have suggested that it knew that the Workers were a species of employee. However, its failure to withhold indicates that it did not think that the Workers were a special breed of employee; it simply thought that they were not employees at all. That was underscored when Microsoft told its managers about the status of the Workers. *See* Microsoft Manager's Handbook 4.7-4.8 (1988). It distinguished the Workers from other employees, both regular full-time and temporary. If did not say that the Workers were employees in some special category; rather, it said that they were not employees at all. *See id.*

But they were employees, which returns us to the contracts themselves. Viewed in the proper light, it can be seen that the Workers were indeed hired by Microsoft to perform services for it. We know that their services were rendered in their capacities as employees. The contracts indicate, however, that they are independent contractors, which they were not. The other terms of the contracts do not add or subtract from their status or, indeed, impose separate agreements upon them. In effect, the other terms

merely warn the Workers about what happens to them if they are independent contractors. Again, those are simply results which hinge on the status determination itself; they are not separate freestanding agreements. Therefore, the Workers were employees, who did not give up or waive their rights to be treated like all other employees under the plans. The Workers performed services for Microsoft under conditions which made them employees. They did sign agreements, which declared that they were independent contractors, but at best that declaration was due to a mutual mistake, and we know that even Microsoft does not now seek to assert that the label made them independent contractors.

On the contrary, Microsoft intended that the Workers perform services under the conditions in question, and they agreed to do so. The parties' intentions were in perfect accord in that respect, and the independent contractor label was a mere error. We see no reason to embrace and perpetuate that error. It could be argued that we would have to reform the contracts in order to elide the mutual mistake. Reformation is a concept available under the law of Washington, as it is elsewhere. *See Wilson v. Westinghouse Elec. Corp.*, 85 Wash.2d 78, 84-85, 530 P.2d 298, 301-02 (1975); *Denny's Restaurants, Inc. v. Security Union Title Ins. Co.*, 71 Wash.App. 194, 212, 859 P.2d 619, 629-30 (1993); *cf. Scott v. Petett*, 63 Wash.App. 50, 57-58, 816 P.2d 1229, 1234-35 (1991). But Microsoft saved us and the Workers the trouble of applying reformation doctrine when it agreed that the Workers were, in fact, not independent contractors. Thus, the label became meaningless, as did the explication of what would follow from that label—no withholding, no benefits.

A similar case from the Eleventh Circuit lends support to our conclusion. *See Daughtrey v. Honeywell, Inc.*, 3 F.3d 1488 (11th Cir. 1993). In *Daughtrey*, the plaintiff had gone to work for Honeywell and had signed an agreement which stated that she was an independent contractor, that she was not an employee, and that she was not "entitled to any benefits or privileges provided by HONEYWELL to its employees." *Id.* at 1490. She later claimed that was entitled to certain ERISA benefits because she was, in fact, an employee. The district court granted summary judgment against her on the theory that she was actually an independent contractor, but the Eleventh Circuit reversed. It did so because it found the facts to be in dispute on that status issue. It seems apparent that what made her status an issue of material fact was that she would be entitled to "employee benefits for the period during which she performed services as a consultant," if she was an employee. *Id.* at 1493. Similarly, in this case, other things remaining equal, it would appear that the Workers are entitled to the benefits of all other employees, or, at least, they are not excluded simply because of the contractual terms.

One additional matter must detain us for a moment. It could, perhaps, be argued that the statements about benefits, unlike statements about withholding, stand on their own footing as a waiver of benefits, regardless of the Workers' true status as employees. As we have said, we think that would be an incorrect interpretation of these agreements, and Microsoft assured us at argument that this is not a waiver case. Were it one, we would have to consider whether the waivers based, as they would have been, on the mistaken premise of independent contractor status were knowing and voluntary under ERISA and Washington law. *See, e.g., Laniok v. Advisory Comm.*, 935 F.2d 1360, 1367 (2d

Cir.1991) (ERISA); *Yakima County (West Valley) Fire Protection Dist. No. 12 v. City of Yakima*, 122 Wash.2d 371, 384, 858 P.2d 245, 252 (1993) (Washington law). Moreover, at least as far as the SPP is concerned, we would have to consider whether the mistaken waiver must and would withstand special scrutiny designed to prevent potential employer or fiduciary abuse. *See, e.g., Sharkey v. Ultramar Energy Ltd.*, 70 F.3d 226, 230-31 (2d Cir. 1995) (close scrutiny used); *Smart v. Gillette Co. Long-Term Disability Plan*, 70 F.3d 173, 181-82 (1st Cir.1995) (careful scrutiny used); *Leavitt v. Northwestern Bell Tel. Co.*, 921 F.2d 160, 162 (8th Cir.1990) (release reviewed to assure no breach of fiduciary duty); *cf. Holt v. Winpisinger*, 811 F.2d 1532, 1541 (D.C. Cir.1987) (ERISA vesting provisions cannot be waived); *Amaro v. Continental Can Co.*, 724 F.2d 747, 752 (9th Cir.1984) (ERISA's minimum standards cannot be waived). However, these issues need not even be mooted once it is recognized that there was no separate waiver at all. Moreover, we need not consider what the result would be if the agreements were of a different form or character.

In short, Microsoft has already recognized that the Workers were employees and that the "no withholding" consequence of the independent contractor label has fallen; we now hold that the "benefit" consequence has fallen also. Having thus burned off the brumes which threatened to obscure our view, we will now turn to the plans themselves.

II. THE PLAN.

A. The SPP.

The SPP is an ERISA plan. *See* 29 U.S.C. § 1002(2)(A)(ii); 26 U.S.C. § 401(k); *In re Dunn*, 988 F.2d 45,

46 (7th Cir.1933). The Workers seek enforcement of the terms of that plan. That is, they seek to have us review the determination of the plan administrator and to require that the plan make its benefits available to them. *See* 29 U.S.C. § 1132(a)(1)(B). As we have already pointed out, the administrative panel of the SPP determined that the Workers are not entitled to benefits. The reasons appear to have been that the Workers were independent contractors and that they waived the benefits. We must review those determinations to see if they were arbitrary or capricious. *See Snow*, 87 F.3d at 330. Based upon what we have already said, it is pellucid that they were. To the extent that the decision was based upon the supposed independent contractor status of the Workers, the plan conceded that the decision was wrong when it conceded that the Workers were, in fact, employees. To the extent that the decision was based upon a supposed waiver of benefits, the plan administrator purported to construe the agreements rather than the plan itself. But, as we have pointed out, our construction is the opposite. We, therefore, determine that the reasons given for denying benefits were arbitrary and capricious because they were based upon legal errors which "misconstrued the Plan and applied a wrong standard to a benefits determination." *Saffle*, 85 F.3d at 461.

The SPP now concedes as much, but it and the Workers asked the district court, and ask us, to decide a different issue of plan construction, one on which the administrator has not opined. The district court accepted that invitation, so did the panel. *See Vizcaino I*, 97 F.3d at 1193. We are tempted to do the same, but upon reflection we have determined that we should not allow ourselves to be seduced into making a decision which belongs to the plan administrator in the first instance.

We are asked to decide what is meant by the SPP's restriction of benefits to common law employees who are "on the United States payroll of the employer." The panel explored some of the reasonably possible meanings of that phrase and construed the apparent ambiguity in favor of the Workers. *See id.* at 1193-96. No doubt the plan administrator should pay careful attention to what was said there. We have also pointed out that we are dubious about the proposition that Microsoft would manipulate plan coverage by assigning recognized common law employees to its accounts payable department or to its payroll department, as it saw fit. We have our doubts that it could properly do so. But it is the terms of the SPP which control, and the plan is separate from Microsoft itself. Thus, we cannot, and will not, predict how the plan administrator, who has the primary duty of construction, will construe terms of the SPP.

We do not know whether he will rely upon an "is" construction—you must actually be on the payroll—or upon an "ought" construction—you must be a person who should be on the payroll. Nor do we know if he will accept the domestic versus foreign gloss on the provision in question. What we do know is that the decision is his in the first instance. We would set a poor precedent were we to intrude upon that exercise of discretion before he has even considered and ruled upon the issue. We would encourage the dumping of difficult and discretionary decisions into the laps of the courts, although one of the very purposes of ERISA is to avoid that kind of complication and delay. Of course, should he rule in favor of the Workers' position, he must then go on to determine what benefits they are entitled to and under what conditions, but that, too, is exactly the kind of decision that he should be making for each of the Workers in the first instance.

We are aware of and do not resile from our decision in *Nelson v. EG &G Energy Measurements Group, Inc.*, 37 F.3d 1384 (9th Cir.1994). However, that case presented us with a somewhat unusual set of facts. In *Nelson* the Administrative Committee had not construed the particular provision, but, more than that, an attempt had been made to induce the Committee to rule on the claims, and that request was rejected out of hand. *See id.* at 1388. Moreover, while the litigation was in progress, the plaintiffs again attempted to induce the Administrative Committee to rule, but that approach was also rebuffed. *See id.* at 1388-89. Given that recalcitrance, we decided that we would determine the issue ourselves and would decide it *de novo* because there was no exercise of discretion to defer to. *See id.* at 1389. That is not this case; this is simply a case where a wholly new issue, which was never put to the SPP administrator, has been raised. He has both the right and the duty to decide it, and we must then review his ultimate decision regarding the Workers by the usual standard. "'It is not the court's function *ab initio* to apply the correct standard to [the participant's] claim. That function, under the Plan, is reserved to the Plan administrator.'" *Saffle*, 85 F.3d at 461 (citation omitted).

B. The ESPP.

The ESPP was a plan adopted for the purpose of taking advantage of the benefits conferred under 26 U.S.C. § 423. It was approved by the board of directors and by the shareholders of Microsoft. Their action was an offer to employees, as that term is defined in § 423. As we have already suggested, we doubt that the corporate officers set out to withdraw the offer from some employees, even if they could have done that. The Workers knew about the fact of

that offer, even if they were not aware of its precise terms. Under the law of the State of Washington, which all agree applies here, a contract can be accepted, even when the employee does not know its precise terms. *See Dorward v. ILWU-PMA Pension Plan*, 75 Wash.2d 478, 452 P.2d 258 (1969). In *Dorward* the court pointed out that a pension is not a gratuity, but "rather is deferred compensation for services rendered." *Id.* at 483, 452 P.2d at 261. We think that that same form of reasoning applies to all employee benefits. Few of them are mere gratuities or a result of unadulterated altruism. Most are for services rendered or for the purpose of inducing the further rendering of services. They help to guarantee a competent and happy labor force. The Washington Supreme Court went on to say:

> The consideration rendered for the promise in the pension contract of the employer to pay a pension is established when the employee is shown to have knowledge of the pension plan and continues his employment. An enforceable contract will arise in such instances even though the pensioner does not know the precise terms of the pension agreement.

Id. Again, we are confident that the court would apply the same reasoning to this employee benefit. Other of its decisions confirm us in our opinion, for it has adopted a protective view toward employees' rights. *See Bowles v. Washington Dep't of Retirement Sys.*, 121 Wash.2d 52, 67-68, 847 P.2d 440, 448 (1993) (pension benefit rights enforced for public employees, even in the absence of specific expectations); *Culinary Workers & Bartenders Union No. 596 Health & Welfare Trust v. Gateway Cafe, Inc.*, 91 Wash.2d 353, 368, 588 P.2d 1334, 1344 (1979) (pension and welfare benefit promises enforced for employees as third-

party beneficiaries); *Jacoby v. Grays Harbor Chair & Mfg. Co.*, 77 Wash.2d 911, 915, 468 P.2d 666, 669 (1970) (where employee knows that a pension plan exists, continued employment is consideration).

The ESPP was created and offered to all employees, the Workers knew of it, even if they were not aware of its precise terms, and their labor gave them a right to participate in it. Of course, Microsoft's officers would not allow that participation because they were under the misapprehension that the board and the shareholders had not extended the offer to the Workers. That error on the officers' part does not change the fact that there was an offer, which was accepted by the Workers' labor. Of course, the ESPP provides for a somewhat unusual benefit. An employee, who chooses to participate, must pay for any purchase of stock, and the Workers never did that. We, however, leave the determination of an appropriate remedy to the district court.[2]

CONCLUSION

Microsoft, like other advanced employers, makes certain benefits available to all of its employees, who meet minimum conditions of eligibility. For some time, it did not believe that the Workers could partake of certain of those benefits because it thought that they were independent contractors. In that it was mistaken, as it now knows and concedes.

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[2] We fully agree with the panel's disposition of Microsoft's asthenic claim that the Workers are attempting to remedy a violation of § 423 itself; we need not repeat the panel's discussion here. *See Vizcaino I*, 97 F.3d at 1197.

The mistake brought Microsoft difficulties with the IRS, but it has resolved those difficulties by making certain payments and by taking other actions. The mistake has also brought it difficulties with the Workers, and the time has come to resolve those.

Therefore, we now determine that the reasons for rejecting the Workers' participation in the SPP and the ESPP were invalid. Any remaining issues regarding the rights of a particular worker in the ESPP and his available remedies must be decided by the district court upon remand. However, any remaining issues regarding the right of any or all of the Workers to participate in the SPP must be decided by the plan administrator upon remand.

REVERSED and REMANDED to the district court as to the ESPP. REVERSED and REMANDED to the district court for further remand to the plan administrator as to the SPP.

FLETCHER, Circuit Judge, with whom HUG, Chief Judge, and PREGERSON, MICHAEL DALY HAWKINS and THOMAS, Circuit Judges, join, concurring in part and dissenting in part:

We concur in the substance of Judge Fernandez' opinion except that we would not remand the issue of eligibility to participate in the SPP to the Plan Administrator and would hold that the Workers are eligible to participate. Remand is inappropriate and further unnecessary in that we conclude that interpretation of the phrase "on the United States payroll of the employer" is not required.

In its denial of the Workers' claim, the administrative panel convened by the Plan Administrator stated:

> The denial is affirmed for the reasons that: (1) claimants had agreed and/or acknowledged upon first working for Microsoft that they would not receive employee benefits; (2) claimants specifically waived (by contract) any rights to benefits and (3) even if claimants had been employees and had not "waived rights to benefits," they were not "regular, full-time employees" in an approved headcount position.

We agree with Judge Fernandez that these determinations were arbitrary and capricious. On appeal, as Judge Fernandez has also properly noted, the Plan abandoned all of its prior positions in favor of a new tack: that the Workers are not eligible for SPP benefits based on a construction of the phrase "on the United States payroll of the employer." Our disagreement with Judge Fernandez, therefore, concerns (1) whether the Plan can properly raise a theory on judicial review not raised in the administrative process, and (2) if a new theory can be raised, whether the appropriate course is for the court to remand to the Plan Administrator to interpret the phrase in the first instance or for the court to decide the issue *de novo*. We would hold that the Plan waived any arguments not raised in the administrative process. Second, we conclude that because of their conduct in this litigation the defendants should be estopped from asserting that remand is appropriate. Third, were we to reach the U.S. payroll question, we would conclude that the issue was resolved by the administrative panel's factual determinations. Finally, were we required to interpret the phrase, we would affirm the interpretation of the original three-judge panel of our court.

I.

Remand to the Plan Administrator to determine the meaning of the phrase "on the United States payroll of the employer" is improper because a plan should not be permitted to assert on judicial review reasons for denial that were not contained in the plan administrator's decision. Because it was raised for the first time before the district court, the Plan Administrator waived this argument.

An ERISA plan is required to:

> provide to every claimant who is denied a claim for benefits written notice setting forth in a manner calculated to be understood by the claimant: (1) The specific reason or reasons for the denial; (2) Specific reference to pertinent plan provisions on which the denial is based; (3) A description of any additional material or information necessary for the claimant to perfect the claim and an explanation of why such material or information is necessary; and (4) Appropriate information as to the steps to be taken if the participant or beneficiary wishes to submit his or her claim for review.

29 C.F.R. § 2560.503-1(f).

We recently construed this requirement:

> In simple English, what this regulation calls for is a meaningful dialogue between ERISA plan administrators and their beneficiaries. If benefits are denied in whole or in part, the reason for the denial must be stated in reasonably clear language,

> with specific reference to the plan provisions that form the basis for the denial; if the plan administrators believe that more information is needed to make a reasoned decision, they must ask for it. There is nothing extraordinary about this; it's how civilized people communicate with each other regarding important matters.

Booton v. Lockheed Med. Benefit Plan, 110 F.3d 1461, 1463 (9th Cir.1997).

These regulations "are designed to afford the beneficiary an explanation of the denial of benefits that is adequate to ensure meaningful review of that denial." *Halpin v. W.W. Grainger, Inc.*, 962 F.2d 685, 689 (7th Cir.1992). The requirements "enable the claimant to prepare adequately for any further administrative review, as well as appeal to the federal courts." *Id.* (internal quotation marks omitted).

In concluding that "no plan can provide discretion to deny benefits for reasons identified only years after the fact," the Seventh Circuit noted that "[t]his Court would emasculate ERISA's disclosure requirement if it were to defer to reasons that the Board first identified on appeal in the District Court, years after the decision at issue." *Matuszak v. Torrington Co.*, 927 F.2d 320, 322-23 (7th Cir. 1991).

This reasoning is sound. One of the fundamental precepts of appellate analysis is review based on a closed record. To allow a plan to raise new reasons for denial on judicial review could subject the plan participant to a cycle of multiple appeals. It would also effectively eviscerate the requirements of ERISA regulations.

In a similar context, we have held that administrative agencies are bound by the reasons stated in their FOIA denial letter and cannot conjure up new reasons on judicial review. *Friends of the Coast Fork v. United States Dep't of the Interior*, 110 F.3d 53, 55 (9th Cir.1997). Because the Plan may not properly raise the U.S. payroll issue for the first time on judicial review, that issue has been waived and it is improper to remand to the Plan Administrator. Accordingly, because the Plan abandoned its other reasons for denying eligibility, the Workers should be entitled to participate in the SPP.

II.

Even if the U.S. payroll issue can be raised on judicial review, the court should decide the issue *de novo* rather than remanding to the Plan Administrator. We conclude that through their conduct in the litigation the defendants should be estopped from asserting that the issue is properly before the Administrator in the first instance. The defendants raised their argument that the Workers were not eligible because they were not on the "United States payroll of the employer" for the first time before the district court and urged that court, initially over the objections of the Workers, to decide the issue. The district court obliged. The defendants not only did not object to the district court deciding the question but affirmatively urged it to do so, and the Workers withdrew their objection. The Workers appealed the decision of the district court to this court. Once again, the defendants urged the court to interpret the phrase and to affirm the district court. The original panel did so but reversed the ruling of the district court and held for the Workers. Only then, after losing on the merits on appeal, in their petition for rehearing and suggestion for

rehearing en banc, do the defendants for the first time argue that we should remand the question of the interpretation of the phrase "on the United States payroll of the employer" to the Plan Administrator if we are unwilling to affirm the district court. The defendants make this argument despite their failure to raise the issue during the administrative process, despite their *sua sponte* raising the issue and urging that it be decided by the district court, and despite their urging that this court reach the issue on appeal. After proceeding through four years of litigation urging at every turn that the issue be decided by the court, the defendants should be estopped from asserting otherwise. *See Voliva v. Seafarers Pension Plan,* 858 F.2d 195, 197 (4th Cir. 1988) ("the party who introduced new evidence in the district court ... cannot argue that the district court was foreclosed from considering the Plan's alternative argument").

Even today the defendants are willing to have us interpret the phrase, but only if we defer to the Administrator. The defendants contend that their willingness to have the court decide the issue all along was contingent upon the court giving deference to their interpretation of the phrase because they represent the Plan. This argument is specious. Although we defer to the reasonable interpretations of a plan administrator when the plan grants the administrator discretion to construe its provisions, *see Firestone Tire & Rubber Co. v. Bruch,* 489 U.S. 101, 111, 109 S.Ct. 948, 103 L.Ed.2d 80 (1989), we do not grant the same discretion to the position taken by a plan as litigant. Where a plan administrator has not exercised his discretion to construe a provision in a plan, our review is *de novo. Nelson v. EG & G Energy Measurements Group, Inc.,* 37 F.3d 1384, 1389 (9th Cir. 1994) (de novo interpretation of plan is appropriate when, although administrative

committee had discretion to do so, it failed to interpret the plan after repeated requests from participants). When conducting *de novo* review we "construe [the terms of a plan] without deferring to either party's interpretation." *Firestone*, 489 U.S. at 112, 109 S. Ct. at 955.

III.

Were we to reach the U.S. payroll issue on *de novo* review, we would hold that the Workers are eligible to participate in the SPP. The case can be resolved without interpreting the Plan language. A careful review of the record before the administrative panel convened by the Plan Administrator reveals that while the administrative panel had no occasion to construe the U.S. payroll language, it did find that the Workers had been "recharacterized, *for payroll purposes only*, . . . as 'employee[s].'" (Emphasis added.) The administrative panel described this recharacterization as follows: "The effect of the IRS's recharacterization is that individuals who had worked in recharacterized positions were issued W-2 forms and they became eligible to refile their income tax returns for the relevant years as 'employees' rather than as 'independent contractors.'"

Because the administrative panel's determination is supported by ample evidence in the record, we should accept its factual determination that the Workers were placed on the payroll of the employer, albeit retroactively, for the relevant period. *Snow v. Standard Ins. Co.*, 87 F.3d 327, 331 (9th Cir. 1996) (reviewing courts must accept the factual determinations of the administrator unless they are clearly erroneous). In light of the administrative panel's finding of fact that the Workers were on the payroll, they are eligible under the SPP regardless of how the "on the United States

payroll" phrase is construed. If, as the Workers suggest, the phrase refers to those employees who are United States residents paid from United States sources, then the Workers would be eligible to participate in the Plan. Alternatively, if the defendants' construction is correct and the phrase limits benefits to those employees who were "on the payroll," then the Workers also prevail. The pleadings establish that the Workers were all United States residents and worked in the United States, and the administrative decision established that they were reclassified as employees on the payroll of the employer. Therefore, under either interpretation the Workers are eligible to participate in the SPP.

IV.

Finally, were we called upon to interpret the phrase we would agree with the conclusion of the original three-judge panel of our court that the Workers are "on the United States payroll of the employer" for substantially the same reasons advanced by the panel. *Vizcaino v. Microsoft,* 97 F.3d 1187, 1196 (9th Cir.1996).

Accordingly, we respectfully dissent from the decision to remand this aspect of the appeal back to the Plan Administrator.

O'SCANNLAIN, Circuit Judge, joined by CYNTHIA HOLCOMB HALL and T.G. NELSON, Circuit Judges, concurring in part and dissenting in part:

I respectfully dissent from all but Part II-A of the court's opinion because Microsoft and the plaintiffs never formed a valid contract under Washington law for the benefits now

claimed. I concur in the result of Part II-A of the court's opinion but not in its analysis.

I.

I do not disagree with the court's statement of facts, but it has failed to mention some and may leave a mistaken impression of others. Thus, I suggest that the following additional facts from the record be taken into account.

The plaintiffs were temporary "freelancers" for Microsoft. Instead of calling them by this label – which was ubiquitously used within the Microsoft community and by the plaintiffs themselves – the court styles the plaintiffs as "workers." It then engages in a long discussion of why they were in fact "common law employees" of Microsoft. Both labels may be true–the plaintiffs did work, and Microsoft has conceded that the plaintiffs satisfy the definition of common law employees for some purposes. Neither of these labels are relevant to the question before us, however, and both are potentially misleading. Both labels imply that the plaintiffs were just like any other regular Microsoft employees, and hence should be eligible for the same benefits as regular staff. The evidence in the record, however, points to the contrary. I will refer to the plaintiffs by the same term the plaintiffs themselves use: "freelancers".

Before going further, it is also important that the statement of facts identify precisely what period of activity is at issue in this case. All plaintiffs were hired before 1989. In the fall of that year, the IRS determined, for employment tax purposes, that the freelancers were common law employees. After that, in late 1989 and during 1990,

Microsoft directly hired some of the freelancers as "staff"[1] (with Microsoft benefits) and arranged for the remainder to become employees of unrelated employment agencies (without Microsoft benefits) who had contracts with Microsoft.[2] For the sake of clarity, I note that all we decide today is whether the freelancers should have been allowed to participate in the ESPP and the SPP during the period leading up to the 1989-90 conversion. All agree that those freelancers who were converted into employees of outside employment agencies have no valid claim for participation in the ESPP and SPP after the date of their conversion.

When the freelancers were originally retained by contract with Microsoft, they were expressly told that they were not eligible for any Microsoft employee benefits, and that they would have to provide their own benefits. Indeed, the named plaintiffs admit that they did not think they were entitled to benefits, and did not think benefits were a part of their compensation package.

Moreover, the freelancers each signed contractual documents which expressly stated that they would not receive any benefits, and would have to pay their own taxes and benefits. Specifically, Microsoft required that each plaintiff sign an "Independent Contractor Agreement" ("ICA"). I think it is appropriate to set out the complete text of the relevant ICA provision:

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[1] "Staff" was the term Microsoft and the plaintiffs use for regular employees.

[2] As the court's opinion notes, a few of the freelancers refused to accept jobs with outside employment agencies. As a result, their relationship with Microsoft ceased altogether.

> CONTRACTOR is an independent contractor for MS [Microsoft]. Nothing in this Agreement shall be construed as creating an employer-employee relationship, or as a guarantee of a future offer of employment. CONTRACTOR further agrees to be responsible for all federal and state taxes, withholding, social security, insurance and other benefits.

Attached to the ICA was a one-page document entitled "independent contractor/freelancer information," which the freelancers also signed. It stated:

> [A]s an Independent Contractor to Microsoft, you are self-employed and are responsible to pay all your own insurance and benefits.

In the district court, Microsoft's uncontested extrinsic evidence established that the plaintiffs were told, and knew, that benefits were not a part of their compensation. Instead of providing benefits, Microsoft paid the freelancers at a higher hourly rate than Microsoft's regular employees. The freelancers were also treated differently in a host of other ways. They had different color employee badges, different e-mail addresses, and were not invited to company parties and functions. Instead of receiving a regular paycheck from Microsoft's Payroll department (like Microsoft's regular employees), freelancers submitted invoices for their services to the Accounts Payable department.

With these additional relevant facts in mind, we may consider the merits.

II.

As I see it, this is a simple case. The Washington law of contracts governs the freelancers' claim of entitlement to benefits under the Employee Stock Purchase Plan ("ESPP"). No law, state or federal, mandates that Microsoft provide such benefits even to its employees. Plaintiffs are eligible to participate in the ESPP only to the extent that they entered into a valid contract with Microsoft for such participation.

Offer, acceptance, and consideration are requisites to contract formation under Washington law. *Thompson v. St. Regis Paper Co.*, 102 Wash.2d 219, 685 P.2d 1081, 1087 (1984). In order to be entitled to benefits under the ESPP, therefore, Microsoft must have offered the benefits to the freelancers, and the freelancers must have accepted that offer.

The court claims that Microsoft's board of directors offered ESPP benefits to the freelancers when they promulgated the ESPP, reasoning that an offer of benefits in a pension plan extends to and may be accepted by employees who do not know its precise terms, as long as they generally know of its existence, citing *Dorward v. ILWU-PMA Pension Plan*, 75 Wash.2d 478, 452 P.2d 258, 261 (1969). The ESPP is not a pension plan, however, and, therefore, standard principles of contract law govern. Even so, as a matter of contract law, *Dorward* might have supported the result in this case if Microsoft's board had merely promulgated the ESPP and the freelancers, knowing of its existence, satisfied the ESPP's eligibility requirements. But in a line of general employment law cases apparently ignored by the court's opinion, Washington courts have held that an employer revokes a generally promulgated offer

when it enters into a specific agreement with an employee which is inconsistent with the offer. *Thompson v. St. Regis Paper Co.*, 102 Wash.2d 219, 685 P.2d 1081, 1087 (1984); *Hill v. J.C. Penney, Inc.*, 70 Wash.App. 225, 852 P.2d 1111, 1117 (1993); *Grimes v. Allied Stores Corp.*, 53 Wash.App. 554, 768 P.2d 528, 529-30 (1989); *see also Swanson v. Liquid Air Corp.*, 118 Wash.2d 512, 826 P.2d 664, 672 (1992) ("It is generally recognized that an employer can disclaim what might otherwise appear to be enforceable promises in handbooks or manuals or similar documents."). As a matter of standard contract law, that principle is unassailable: an offer can be revoked by giving specific notice to the offeree at any time prior to acceptance or substantial performance. *Collins v. Morgan Grain Co.*, 16 F.2d 253, 255 (9th Cir. 1926), cited with approval in 1 Arthur L. Corbin & Joseph M. Perillo, *Corbin on Contracts*, § 2.18, at 217 n. 7 (rev. ed. 1993). And, after all, the Washington Supreme Court has clearly proclaimed that the traditional requisites of contract formation apply with full force to modern, unilateral employment contracts. *Thompson*, 685 P.2d at 1087.

Exactly such a revocation occurred here. Microsoft's board offered the ESPP to employees generally, and then Microsoft told the freelancers: "We aren't offering the ESPP to you; ESPP benefits are not included in your contract." Knowing that they wouldn't get ESPP benefits, the freelancers nevertheless agreed to work for Microsoft. Their contract therefore does not include ESPP benefits because the offer of those benefits was revoked.

Likewise, there was no mutual assent (or "meeting of the minds") as is required for the formation of a unilateral contract. *See Multicare Medical Center v. State*, 114 Wash.2d 572, 790 P.2d 124, 132-33 (Wash. 1990). Microsoft did not

think it was offering ESPP benefits to the freelancers, and the freelancers did not think they were accepting an offer of ESPP benefits. Had the parties known that a court would force them to include ESPP benefits in their contract, the bargain undoubtedly would have been different.

If this is not enough, the court's alleged contract suffers from another defect: a lack of consideration. There was no detrimental reliance on the ESPP by the freelancers–they did not think they would get ESPP benefits, and they still chose to work for Microsoft on Microsoft's terms. Indeed, it is hard to imagine what consideration the freelancers could have given for the ESPP benefits since they chose to work for Microsoft for several years without benefits. If anything, the freelancers received consideration (a higher hourly rate) for their agreement that they would *not* get ESPP benefits.

The court conjures up two reasons to disregard the express and unambiguous revocation of the offer of benefits to the workers, and to find a contract for benefits where none exists. First, the court says, the statements in the employment contracts were the result of a mistake since Microsoft's officers incorrectly thought the freelancers were independent contractors. The statements were not meant to have independent legal significance, but were "simply a helpful disclosure" explaining the meaning of independent contractor status—a status, it later turns out, that the freelancers did not have. I am unpersuaded.

The court makes this simple contracts case unnecessarily complicated, obfuscating the obvious meaning of the agreements. When one sets the ESPP side-by-side with the agreement signed by the freelancers, one realizes that no brumes obscure the court's view of a solution to its

manufactured mistake; it vainly scans the horizon for a solution which is sitting right under its nose. Microsoft drafted the ESPP and the agreements using the same terminology ("employee") to ensure there could be no mistaking that ESPP benefits were not part of the bargain. The signed agreements say: "Nothing in this Agreement shall be construed as creating an employer-employee relationship. . . . CONTRACTOR further agrees to be responsible for all . . . benefits." These provisions are not simply a "helpful disclosure." Quite the contrary, the agreement says "CONTRACTOR further agrees ..." How much clearer could it be that this is an independent, legally binding part of the bargain? By "burning off" this inconvenient contract language, the court may as well have set fire to the contracts themselves.

To top it off, Washington courts have already rejected the court's reasoning. In *Daniel v. Pacific Northwest Bell Telephone Co.*, 20 Wash.App. 444, 580 P.2d 652, 654 (1978), a worker signed a written agreement with the telephone company stating that he was an independent contractor, although under the common law definition, the worker was in fact an employee. The Washington court ruled that the common law definition was inapposite:

> It is well settled that one is bound by the contract which he voluntarily and knowingly signs. It has been said that "the whole panoply of contract law rests on . . . [that] principle . . ." *National Bank of Washington v. Equity Investors,* 81 Wash.2d 886, 912-13, [506 P.2d 20] (1973). For 18 years, the contract under which Mr. Daniel performed his work declared that he was an independent contractor. He does not claim that he did not

> understand the meaning of that term, nor does he contend that the contracts were the result of overreaching or fraud by the telephone company. In these circumstances, the characterization of Mr. Daniel's employment as that of an independent contractor is binding as between Mr. Daniel and the telephone company.

Id. This court's discussion of common law employees and mutual mistakes should be seen for what it is—a smokescreen which both confuses and conceals. Regardless of whether Microsoft and the freelancers were mistaken about the freelancers' employment status, their agreement stands on its own and ought to be enforced according to its terms.

The court's second argument, albeit not fully developed, is that under Delaware's corporations law, Microsoft's officers did not have authority to modify or to revoke the offer of the ESPP made by Microsoft's board of directors. There are two problems with this analysis.

First, as an entity without a physical existence, Microsoft can only act through its agents. *Conklin Bros., Inc. v. United States,* 986 F.2d 315, 318 (9th Cir. 1993). Under Delaware's corporations law, however, the board of directors directs the affairs of the business but is not an agent of the corporation. *Arnold v. Society for Savings Bancorp, Inc.*, 678 A.2d 533, 539-40 (Del. 1996); *see also* Restatement (Second) of Agency § 14C (1958) ("Neither the board of directors nor an individual director of a business is, as such, an agent of the corporation or of its members."). The only way to enter into a contract with Microsoft, therefore, was through Microsoft's officers and employees as

agents of the corporation. It may be that the officers and employees did not have the actual authority to make a "no ESPP benefits" offer to the freelancers. They certainly had the apparent authority to strike such a bargain, however. In any event, under standard principles of agency law, if the principal ratifies unauthorized acts of its agent, the ratification relates back to the time of the acts and is equivalent to original authority. *Hannigan v. Italo Petroleum Corp.*, 47 A.2d 169, 172 (Del. 1945). By accepting the freelancers' performance under the contract, and by choosing to defend against the freelancers' claim from 1990 until now, Microsoft's board of directors, and Microsoft itself, has impliedly ratified the "no ESPP benefits" offer. *See id.* Delaware law is therefore no obstacle to a contract for no ESPP benefits.

Second, even if the officers did not have the actual authority under Delaware corporations law to make a "no ESPP benefits" offer to the freelancers, the contract formed by the freelancers' acceptance of the offer exists nonetheless. The "no benefits" provision is an important term of the overall contract and should not be treated apart from the bargain as a whole. The freelancers cannot, with perfect hindsight, pick and choose among the parts of the contract they want to enforce while discarding the provisions they don't like, premised upon the notion that the officers lacked authority to form the contract. Furthermore, a contrary ruling undermines Delaware's carefully crafted rule that only the corporation (or a shareholder suing derivatively) can seek a remedy for unauthorized acts of corporate officers. *See Dieter v. Prime Computer, Inc.*, 681 A.2d 1068, 1072 (Del.Ch. 1996).[3]

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[3] Similarly, that the board's ratification might have adverse tax

(continued...)

III.

The freelancers also claim that Microsoft should have allowed them to participate in its Savings Plus Plan ("SPP"), which is governed by ERISA. The SPP provides that "[e]ach employee who is 18 years of age or older and who has been employed for six months shall be eligible to participate in this Plan." It then defines "employee" as "any common law employee who receives remuneration for personal services rendered to the employer and who is on the United States payroll of the employer." The freelancers argue that they fit this definition of employee; Microsoft retorts that the freelancers were not "on the United States payroll of the employer." Our first task, therefore, is ascertaining what that phrase means.

We cannot immediately set about this task, however, because the SPP grants discretion to the plan administrator to construe the plan. The Supreme Court has instructed us that when the plan vests discretion in the administrator, principles of trust law require that we leave the plan administrator's interpretation undisturbed if reasonable. *Firestone Tire & Rubber Co. v. Bruch,* 489 U.S. 101, 111, 109 S.Ct. 948, 954-55, 103 L.Ed.2d 80 (1989). Indeed, ERISA encourages plan fiduciaries to exercise properly the discretion they have been granted; courts should not be second-guessing the discretionary decisions of fiduciaries without a very good reason. Thus, we are not to impose our view of a provision on the plan, but are confined to reviewing

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[3] (...continued)
consequences for the ESPP does not allow us to ignore the overwhelming evidence that the officers and the board did not offer ESPP participation to the freelancers.

the administrator's instruction to determine whether it is reasonable.

In order for this rule protecting a plan administrator's discretion to be meaningful, however, the administrator must be given an opportunity to interpret the meaning of plan provisions before the court rules. In this case, the plan administrator did not overtly construe the phrase "on the United States payroll of the employer," at least so far as I can tell from the record. The district court believed that the administrator impliedly rested its decision on a particular interpretation of that phrase. Although there is a colorable argument in support of the district court's belief, I believe that the judicially stated preference that the plan administrator interpret the plan, subject to a limited review by courts, requires us to remand to the plan administrator explicitly to construe the meaning of that phrase. I agree with the court's conclusion on this point.[4]

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[4] Judge Fletcher contends that a remand is inappropriate because (1) the Plan has waived any claim that the provision might bar benefits for the freelancers by not interpreting the Plan provision in the first instance, and (2) the Plan is estopped from arguing for a remand.

With respect, her first argument overlooks the fact that the Plan Administrator had no need to reach the question of the meaning of "on the United States payroll" since it had already determined that the freelancers were not entitled to benefits on several other grounds. I am not persuaded that by failing to interpret expressly a provision in the Plan the Administrator rendered the provision a nullity. Moreover, Judge Fletcher reads this concurrence and dissent too broadly; it does not hold that the Plan or Microsoft should prevail on the merits of an argument never raised before, but only that the Plan Administrator should be given an opportunity to construe a phrase it thought unnecessary to reach.

(continued...)

I write separately to clarify that I do not concur in the court's analysis of the meaning and implications of "on the United States payroll of the employer," and, as dicta, the court's statements do not bind the plan administrator in any way. In my view, that phrase is a term of art with significance within the Microsoft community. Further, I do not agree with the ill-advised suggestion that Microsoft might not have been able properly to classify employees for participation or non-participation in an ERISA plan based on whether the employees were regular hires paid through the Payroll department or "freelancers" paid through the Accounts Payable department. Microsoft could choose to offer the SPP to whichever classes of employees it wishes. It is certainly free to decide not to offer positions satisfying the SPP's criteria to these plaintiffs.

I respectfully concur in the result of Part II-A of the court's opinion but otherwise dissent.

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[4] (...continued)
Judge Fletcher's second argument misapprehends, in my view, the nature of our review in this case. It is not a question of whether the Plan or Microsoft wishes us to decide the question or to remand it; a party cannot, by waiver or estoppel, change the applicable standard of review. Principles of trust law and ERISA limit our review of the Plan Administrator's discretion. We must give the Administrator an opportunity to exercise that discretion by remanding the case. Our conclusion has nothing to do with whether Microsoft urges us to decide the merits.

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

DONNA VIZCAINO; JON R. WAITE; MARK STOUT; GEOFFREY CULBERT; LESLEY STUART; THOMAS MORGAN; ELIZABETH SPOKOINY; LARRY SPOKOINY,	)	No. 94-35770
Plaintiffs-Appellants,	)	D.C. No. CV-93-00178-CRD
v.	)	OPINION
MICROSOFT CORPORATION, and its pension and welfare benefit plans, et al., *Defendants-Appellees.*	)	

Appeal from the United States District Court
for the Western District of Washington
Carolyn R. Dimmick, District Judge, Presiding

Argued and Submitted
October 18, 1995—Seattle, Washington

Filed October 3, 1996

Before: Stephen Reinhardt and Stephen S. Trott, Circuit Judges, and William W. Schwarzer, District Judge.*

* The Honorable William W. Schwarzer, Senior United States District Judge for the Northern District of California, sitting by designation.

Opinion by Judge Reinhardt;
Dissent by Judge Trott

COUNSEL

Stephen K. Strong and David F. Stobaugh, Bendich, Stobaugh & Strong, Seattle, Washington, for the plaintiffs-appellants.

James D. Oswald and Timothy St. Clair Smith, Davies, Roberts & Reid, Seattle, Washington, for the defendants-appellees.

OPINION

REINHARDT, Circuit Judge:

Large corporations have increasingly adopted the practice of hiring temporary employees or independent contractors as a means of avoiding payment of employee benefits, and thereby increasing their profits. This practice has understandably led to a number of problems, legal and otherwise. One of the legal issues that sometimes arises is exemplified by this lawsuit. The named plaintiffs, who were classified by Microsoft as independent contractors, seek to strip that label of its protective covering and to obtain for themselves certain benefits that the company provided to all of its regular or permanent employees. After certifying the named plaintiffs as representatives of a class of "common-law employees," the district court granted summary judgment to Microsoft on all counts. The named plaintiffs and the class they represent now appeal as to two of their

claims: a) the claim, made pursuant to section 502(a) of the Employee Retirement Income Security Act (ERISA), 29 U.S.C. § 1132(a), that they are entitled to savings benefits under Microsoft's Savings Plus Plan (SPP); and b) the claim, made pursuant to Washington state law, that they are entitled to stock-option benefits under Microsoft's Employee Stock Purchase Plan (ESPP). In both cases, the claims are based on their contention that they are common-law employees.

I

Microsoft, one of the country's fastest growing and most successful corporations and the world's largest software company, produces and sells computer software internationally. It employs a core staff of permanent employees. It categorizes them as "regular employees" and offers them a wide variety of benefits, including paid vacations, sick leave, holidays, short-term disability, group health and life insurance, and pensions, as well as the two benefits involved in this appeal. Microsoft supplements its core staff of employees with a pool of individuals to whom it refuses to pay fringe benefits. It previously classified these individuals as "independent contractors" or "freelancers," but prior to the filing of the action began classifying them as "temporary agency employees." Freelancers were hired when Microsoft needed to expand its workforce to meet the demands of new product schedules. The company did not, of course, provide them with any of the employee benefits regular employees receive.

The named plaintiffs worked for Microsoft in the United States between 1987 and 1990 as freelancers in the

company's international division.[1] Some were still working for the company when the suit was filed in 1993, and may still be doing so today. Although hired to work on specific projects, seven of the eight named plaintiffs had worked on successive projects for a minimum of two years prior to the time the action was filed, while the eighth had worked for more than a year. During that time, they performed services as software testers, production editors, proofreaders, formatters and indexers. Microsoft fully integrated the plaintiffs into its workforce: they often worked on teams alongwith regular employees, sharing the same supervisors, performing identical functions, and working the same core hours. Because Microsoft required that they work on site, they received admittance card keys, office equipment and supplies from the company.

Freelancers and regular employees, however, were not without their obvious distinctions. Freelancers wore badges of a different color, had different electronic-mail addresses, and attended a less formal orientation than that provided to

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[1] The district court certified a class comprising

> [a]ll persons employed by Microsoft Corporation in the United States who are denied employee benefits because they are considered independent contractors or employees of third-party employment agencies, but who meet the definition of employees of Microsoft Corporation under the common law.

Microsoft did not object to the class certification or contest the determination that freelancers or independent contractors are proper class members but sought to reserve the question as to whether certain specific individuals fell within the class as well as the question of the amounts due class members by way of benefits or damages. *See* ER at 27. *See also infra* n. 4.

regular employees. They were not permitted to assign their work to others, invited to official company functions, or paid overtime wages. In addition, they were not paid through Microsoft's payroll department. Instead, they submitted invoices for their services, documenting their hours and the projects on which they worked, and were paid through the accounts receivable department.

The plaintiffs were told when they were hired that, as freelancers, they would not be eligible for benefits. None has contended that Microsoft ever promised them any benefits individually. All eight named plaintiffs signed "Microsoft Corporation Independent Contractor Copyright Assignment and Non-Disclosure Agreements" (non-disclosure agreements) as well as companion documents entitled "Independent Contractor/Freelancer Information" (information documents) when first hired by Microsoft or soon thereafter. The non-disclosure agreement, a three-page document primarily concerned with confidentiality, included a provision that states that the undersigned "agrees to be responsible for all federal and state taxes, withholding, social security, insurance and other benefits." The information document likewise states that "as an Independent Contractor to Microsoft, you are self-employed and are responsible to pay all your own insurance and benefits." Eventually, the plaintiffs learned of the various benefits being provided to regular employees from speaking with them or reading various Microsoft publications concerning employee benefits.

In 1989 and 1990, the Internal Revenue Service (IRS) examined Microsoft's employment records to determine whether the company was in compliance with the tax laws. Applying common-law principles defining the employer-

employee relationship, it concluded that Microsoft's freelancers were not independent contractors but employees for withholding and employment tax purposes, and that Microsoft would thereafter be required to pay withholding taxes and the employer's portion of Federal Insurance Contribution Act (FICA) tax.[2] Microsoft agreed to pay overdue employer withholding taxes and issue retroactive W-2 forms to allow the freelancers to recover Microsoft's share of FICA taxes, which they had been required to pay. It apparently also agreed to pay freelancers retroactively for any overtime they may have worked.

In response to the IRS rulings, Microsoft began "converting" its freelancers. That is, it tendered offers to some freelancers to become permanent employees; it gave other freelancers the option of terminating their employment relationship with Microsoft completely or continuing to work at the company but in the capacity of employees of a new temporary employment agency, which would provide payroll services, withhold federal taxes, and pay the employer's portion of FICA taxes. Most of the plaintiffs who were not given the opportunity to become permanent employees decided to become "temporary agency employees" rather than to be fired. However, Donna Vizcaino refused that option and was discharged. Those who elected "temporary

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[2] "[B]ased on information received from Microsoft and on information received from a representative sampling of the workers in that job position," the IRS concluded in one of several letter rulings that because "Microsoft either exercised, or retained the right to exercise, direction over the services performed," those persons employed as testers were employees of Microsoft "for purposes of the Federal Insurance Contribution Act, the Federal Unemployment Tax Act, and for Collection of Income Tax at the Source on Wages." The IRS issued similar findings regarding formatters, proofreaders, and production editors.

employee status" noticed little change in the terms or conditions of their employment; they continued working the same hours on the same projects and under the same supervisors.

After learning of the IRS rulings, the plaintiffs sought various employee benefits, including those now at issue: the ESPP and SPP benefits. The SPP, which became effective January 1, 1987, is a cash or deferred salary arrangement under § 401k of the Internal Revenue Code that permits Microsoft's employees to save and invest up to fifteen percent of their income through tax-deferred payroll deductions. Under the plan, Microsoft matches fifty percent of the employee's contribution in any year, with a maximum matching contribution of three percent of the employee's yearly compensation. The ESPP, established in January, 1986, permits employees to purchase company stock at eighty-five percent of the lower of the fair market value on the first or on the last day of each six-month offering period through payroll deductions of from two to ten percent. Employees may purchase shares having a value not exceeding ten percent of their gross compensation for the offering period.

Microsoft rejected the plaintiffs' claims for benefits, maintaining that they were independent contractors who were personally responsible for all their own benefits. The plaintiffs sought review of the denial of benefits from the Microsoft plan administrator, who determined that the plaintiffs were ineligible because they contractually waived any rights to benefits and, in any event, they were not " 'regular, full-time employees' in approved headcount positions." Although ruling "technically" only on the denial of ERISA benefits, the plan administrator concluded, for the

same reasons, that the plaintiffs were ineligible to receive non-ERISA benefits.

The named plaintiffs brought this action, challenging the denial of benefits. Following cross-motions for summary judgment, the district court referred the matter to Magistrate Judge David E. Wilson, who recommended that an award be made in favor of the plaintiffs on both their SPP and ESPP claims. First, he concluded that the SPP was ambiguous with respect to whether it afforded coverage to the plaintiffs and that because the ambiguity could not be conclusively resolved by resort to extrinsic evidence, the doctrine of *contra proferentem* was applicable. Accordingly, he determined that the plan instruments should be construed in the plaintiffs' favor and recommended that the district court find that the plan afforded them coverage. Second, he concluded that by expressly adopting the conditions of the Internal Revenue Code, which permit tax qualification only to those plans that extend participation to all common-law employees, Microsoft had extended an offer of participation in the ESPP to all common-law employees, and that the plaintiffs fell into that category. Further, he found that although Microsoft had intended to exclude freelancers from participation in the ESPP, it had made the plaintiffs an offer in that plan and could not rely on their failure to accept it because it had incorrectly told them that they were ineligible to participate. Again, the magistrate judge recommended that the district court find that the plaintiffs were eligible for benefits.

The magistrate judge also made recommendations on several motions relating to benefits other than the SPP and ESPP. Specifically, he recommended denying the plaintiffs' motion for summary judgment in relation to vacation, sick

leave, holidays, short-term disability, group health and life insurance, and granting Microsoft's motion for summary judgment on all claims governed by ERISA, except the SPP claim, and on all claims governed by state law, except the ESPP claim.

The district court adopted the magistrate judge's recommendations on all issues other than the SPP and ESPP claims. It rejected his recommendations as to those two claims and denied the plaintiffs' motion for summary judgment as to them, while granting Microsoft's. The district court first concluded that the SPP "clearly restricts participation to those individuals on Microsoft's payroll," that even if Microsoft could waive the argument that only employees paid through the payroll were eligible it had not done so, and that because the intent of the parties was to deny the plaintiff's participation, the terms of the plan were susceptible to only one reasonable interpretation. Thus, it said, the doctrine of *contra proferentem* was not applicable. Then, addressing the plaintiffs' eligibility to participate in the ESPP, the district court concluded:

> First, the contract between Microsoft and the plaintiffs specifically stated that no benefits were provided by Microsoft. Second, because the terms of the plan were not communicated to the plaintiffs, they could not have become part of the contract between them and Microsoft. Thus, the plaintiffs had no expectation of receiving any benefits. Finally, as Microsoft asserts, I.R.C. § 423 does not create a private right of action by the plaintiffs against Microsoft.

The named plaintiffs and the class they represent appeal, but only with respect to the SPP and ESPP claims.

II

ERISA is a remedial statute designed to protect the interests of employees in pension and welfare benefit plans. *Scott v. Gulf Oil Corp.*, 754 F.2d 1499, 1501 (9th Cir. 1985). It creates a federal cause of action for recovery of benefits due under the terms of pension and welfare plans. 29 U.S.C. § 1132(a)(1)(B).[3] Congress intended the courts to fashion a body of federal common law to govern ERISA suits. *Richardson v. Pension Plan of Bethlehem Steel*, 67 F.3d 1462, 1465 (9th Cir. 1995); *Scott*, 754 F.2d at 1501-02. Courts, therefore, may borrow from state law where appropriate, but must be guided by the policies expressed in ERISA and other federal labor laws. *Richardson*, 67 F.3d at 1465; *Scott*, 754 F.2d at 1502.

The parties agree that the SPP is a welfare benefits plan governed by ERISA. *See* 29 U.S.C. § 1002(1)(A). They disagree, however, on the question whether the plaintiffs qualify for benefits under the terms of the plan. The SPP provides that "[e]ach employee who is 18 years of age or older and who has been employed for six months shall be eligible to participate in this Plan," and defines "employee" to mean "*any common-law employee* who receives remuneration for personal services rendered to the employer and *who is on the United States payroll of the employer.*" (Emphasis added). Because the named plaintiffs

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[3] Section 1132(a)(1)(B) provides, in pertinent part, that a "civil action may be brought . . . by a participant or beneficiary . . . to recover benefits due to him *under the terms of the plan* . . . ." (Emphasis added).

were indisputably over eighteen years of age and were employed for more than six months, and because, as Microsoft concedes, they were generally common-law employees who rendered personal services to Microsoft,[4] the issue before us is only whether they were "on the United States payroll of the employer." Microsoft contends that the phrase, which is not defined in the plan, refers to employees paid through its payroll department, and that the named plaintiffs were ineligible to participate in the SPP because they were paid through the accounts receivable department. The plaintiffs assert that the phrase refers to "Microsoft employees who are paid from United States sources," excluding "nonresident alien employees of foreign subsidiaries whose pensions are generally governed by foreign law."

In the usual case, we review a denial of benefits challenged under section 1132(a)(1)(B) *de novo* "unless the benefit plan gives the administrator or fiduciary discretionary authority to determine eligibility for benefits or to construe the terms of the plan." *Nelson v. EG & G Energy Measurements Group, Inc.*, 37 F.3d 1384, 1388 (9th

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[4] As the magistrate judge stated in his Report and Recommendations, Microsoft conceded the fact that the named plaintiffs and the class they represent generally were common-law employees. ER at 144, 147-48. *See also supra* n. 1. Microsoft reserved only the right to object to the employment status of particular plaintiffs during certain periods of their tenure with Microsoft and to contest the amount of damages or benefits to be awarded. CR Vol. 12, Document 152, at 9 n. 5. For example, Microsoft stated that "for some period of time, Plaintiff Morgan performed proofreading services from his home, with an uncertain amount of supervision." *Id.* Questions raising legitimate disputes regarding specific individuals' eligibility are left to the district court for resolution following remand.

Cir. 1994).[5] Where such discretion is afforded, the standard of review may vary with the type or nature of the plan. *Taft v. Equitable Life Assurance Soc'y*, 9 F.3d 1469, 1474 (9th Cir. 1993) (stating that we review decisions of administrators who are also employers of plan beneficiaries under " 'a more *stringent* version of the abuse of discretion standard' ") (citation omitted).

In the case before us, the administrator is a Microsoft officer. We need not, however, determine what standard would ordinarily be applicable to review of a denial of benefits under the SPP. For, while the plan gives the administrator discretion to construe its provisions, in denying the plaintiffs' claims the administrator did not construe the phrase "on the United States payroll of the employer," the phrase in the plan on which eligibility depends. Oddly, Microsoft did not raise its "United States payroll" theory before the plan administrator but argued it for the first time to the magistrate judge in the course of its motion for summary judgement.[6] The plaintiffs initially objected to consideration of the "United States payroll" argument because it did not appear in the administrative record, but then waived the objection and, like Microsoft, urged the magistrate judge and the district judge to address it. Both parties have consistently maintained that a remand to the plan administrator would serve no useful purpose. *See*

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[5] When the plan does not grant the plan administrator discretion to construe its provisions, the district court reviews *de novo*, and our review is also *de novo*. *Mongeluzo v. Baxter Travenol Long Term Disability Benefit Plan*, 46 F.3d 938, 942 (9th Cir. 1995).

[6] Microsoft prevailed before the plan administrator on the theory that the plaintiffs were not "regular, full-time employees" in "approved headcount positions," a theory that it has since abandoned.

CR. Vol. 12, Document 152, at 22-23; CR. Vol. 12, Document 169, at 12 n. 11. Because both parties urged the district court, and now this court, to determine the meaning of the disputed provision, they have waived any possible objection to the failure to remand. Accordingly, we are free to decide Microsoft's latest argument in the normal course, as if the plan administrator had no discretion to construe the plan. *Cf. Nelson*, 37 F.3d at 1389 (holding that our review is *de novo* where the plan administrator, although having discretion to construe the plan, has not done so).[7]

We interpret the provisions of a plan by looking to its terms and to other manifestations of intent. *Nelson*, 37 F.3d at 1389. We interpret terms in ERISA plans " 'in an ordinary and popular sense as would a [person] of average intelligence and experience.' " *Richardson*, 67 F.3d at 1465 (quoting *Evans v. Safeco Life Ins. Co.*, 916 F.2d 1437, 1441 (9th Cir. 1990)); *Babikian v. Paul Revere Life Ins. Co.*, 63 F.3d 837, 840 (9th Cir. 1995); *accord Meredith v. Allsteel Inc.*, 11 F.3d 1354, 1358 (7th Cir. 1993). " 'We will not artificially create ambiguity where none exists. If a reasonable interpretation favors the insurer and any other interpretation would be strained, no compulsion exists to torture or twist the language of the policy.' " *Babikian*, 63

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[7] This case is not controlled by *Saffle v. Sierra Pacific Power Company*, 85 F.3d 455 (9th Cir. 1996). There, we held that where a plan administrator misconstrues a plan, the court should not determine whether benefits are to be awarded under a proper construction; instead, it should remand to the plan administrator for it to make a determination under the plan, properly construed. Here, the term that determines the plaintiff's eligibility was not construed at all by the plan administrator. More important, both parties have agreed that a remand would be inappropriate. The parties are, of course, free to waive any right they may have to a construction by a plan administrator.

F.3d at 840 (quoting *Evans*, 916 F.2d at 1441 (quoting *Allstate Ins. Co. v. Ellison*, 757 F.2d 1042, 1044 (9th Cir. 1985))). We find "[a] term is ambiguous if it is subject to reasonable alternative interpretations." *Hickey v. A.E. Staley Mfg.*, 995 F.2d 1385, 1389 (9th Cir. 1993) (citation and internal quotation marks omitted); *see Babikian*, 63 F.3d at 840.

When a plan is ambiguous on its face, we may, and typically do, consider extrinsic evidence to interpret it. *Richardson*, 67 F.3d at 1466; *Hickey*, 995 F.2d at 1389. If the ambiguity persists even after resort to extrinsic evidence, we generally apply the rule of *contra proferentem* and construe the ambiguity against the drafter. *See Barnes v. Independent Auto. Dealers of Cal.*, 64 F.3d 1389, 1393 (9th Cir. 1995) ("We must construe ambiguities in an ERISA plan against the drafter and in favor of the insured."); *Babikian*, 63 F.3d at 840; *Mongeluzo v. Baxter Travenol Long Term Disability Benefit Plan*, 46 F.3d 938, 942 (9th Cir. 1995) (noting that *Kunin v. Benefit Trust Life Ins. Co.*, 910 F.2d 534, 539-41 (9th Cir.), *cert. denied*, 498 U.S. 1013, 111 S. Ct. 581, 112 L.Ed.2d 587 (1990), adopted the well-established doctrine of *contra proferentem* as federal common law).

Accordingly, our first task is to determine whether the phrase "on the United States payroll of the employer" is susceptible to more than one reasonable interpretation. In doing so, we must examine the phrase in light of any relevant circumstances that may shed light on its meaning. Here, the phrase is used in connection with a company that is engaged in a constantly expanding business venture of major proportions on a world-wide basis. Because "payroll" means "a list of persons to be paid, with the amount due each," or "the total number of people employed by a

business firm or organization," Random House College Dictionary 976 (1980), the phrase "on the United States payroll of the employer," when accorded its ordinary meaning, may plausibly refer to those persons who are on the list of, or are among the total number of, persons employed by Microsoft and paid from its United States accounts, as opposed to those paid by its foreign subsidiaries or out of its foreign accounts. Thus, we believe that the plan, consistent with the ordinary meaning of its terms, reasonably can be read to extend eligibility to the plaintiffs.[8]

While an argument could well be made that the plaintiffs' is the only plausible reading of the plan, we choose not to rely on that assertion. Instead, we assume that Microsoft's interpretation is also a reasonable one, and accept its contention that the phrase could reasonably be construed to refer only to those employees paid through the payroll department. Assuming, then, that the terms of the SPP are susceptible to two reasonable interpretations and therefore are ambiguous, our next step is to determine whether the ambiguity can be resolved by resort to extrinsic evidence.

Microsoft contends that the extrinsic evidence, including the non-disclosure agreements and the information documents, demonstrates its intent not to provide freelancers or independent contractors with employee

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[8] There may be a slight variation on the interpretation set forth above that is equally plausible and would similarly serve to extend eligibility to the plaintiffs. Under that variation, the disputed phrase would be construed as referring to all persons employed by Microsoft in the United States. However, we need not examine that possibility here.

benefits and that this intent necessitates adoption of its interpretation of the disputed phrase. We have no doubt that the company did not intend to provide freelancers or independent contractors with employee benefits, and that if the plaintiffs had in fact been freelancers or independent contractors, they would not be eligible under the plan. The plaintiffs, however, were not freelancers or independent contractors. They were common-law employees,[9] and the question is what, if anything, Microsoft intended with respect to persons who were actually common-law employees but were not known to Microsoft to be such. The fact that Microsoft did not intend to provide benefits to persons who it thought were freelancers or independent contractors sheds little or no light on that question. To the extent that we may glean any evidence of an intent as to the more pertinent theoretical question, that evidence is highly speculative and would be insufficient to resolve in Microsoft's favor the ambiguity that it created when it chose to define eligibility in terms of common-law employees "on the United States payroll of the employer."

Microsoft also contends that extrinsic evidence establishes its intent to restrict eligibility to those common-law employees who were paid through the payroll department. It argues that compliance with relevant tax

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[9] The instruments signed by the plaintiffs label them as independent contractors. Those instruments, however, do not control the plaintiffs' employment status. *See Daughtrey v. Honeywell*, 3 F.3d 1488, 1492 (11th Cir. 1993) ("The employment status of an individual for the purposes of ERISA is not determined by the label used in the contract between the parties."). Accordingly, the label used here does not determine whether the plaintiffs are or are not common-law employees. The record does, and as Microsoft has conceded, the named plaintiffs and those they represent are generally common-law employees.

code provisions (I.R.C. §§ 401(k) & (m)) required computation of compensation, deferral, and matching contribution data, and that the necessary computations could practically be made only through its automated payroll department. It maintains that employees who were paid through the accounts receivable department, as opposed to the payroll department, could not be paid in a manner that would comply with IRS requirements and that, accordingly, it is clear that those employees were not intended to be covered in the plan.

Microsoft's argument, drawing a distinction between common-law employees on the basis of the manner in which they were paid, is subject to the same vice as its more general argument. Microsoft regarded the plaintiffs as independent contractors during the relevant period and learned of their common-law employee status only after the IRS examination. They were paid through the accounts receivable department rather than the payroll department because of Microsoft's mistaken view as to their legal status. Accordingly, Microsoft cannot now contend that the fact that they were paid through the accounts receivable department demonstrates that the company intended to deny them the benefits received by all common-law employees regardless of their actual employment status. Indeed, Microsoft has pointed to no evidence suggesting that it ever denied eligibility to any employees, whom it *understood* to be common-law employees, by paying them through the accounts receivable department or otherwise.

In any event, to interpret the SPP as distinguishing between common-law employees who were paid through the payroll department and those who were not would impute to Microsoft an unlawful purpose: to pay some common-law

employees without making the requisite payroll deductions and contributions, the very tax violation that subsequently engendered this litigation. We should not, if at all possible, favor an interpretation that has such an unlawful effect, and we see no reason to do so here. *See Meredith v. Allsteel, Inc.*, 11 F.3d 1354, 1358 (7th Cir. 1993) ("[A]n interpretation which gives a reasonable, lawful, and effective meaning to all the terms is preferred to an interpretation which leaves a part unreasonable, unlawful, or of no effect[.]") (citation and internal quotation marks omitted). Thus, the extrinsic evidence on which Microsoft relies does nor resolve the ambiguity in its favor.

In light of the rule of *contra proferentem,* the plaintiffs would prevail whether the extrinsic evidence supported their interpretation of the disputed phrase or whether the extrinsic evidence on which they rely was also deemed immaterial. For purposes of our disposition, we may assume the latter to be the case. With that assumption in mind, we find, as did the magistrate judge, that "the correct meaning of the terms in question, given the record and the agreed upon facts in this case, cannot be determined by resort to the extrinsic evidence," and that, therefore, the rule of *contra proferentem* is applicable.

Microsoft contends that the rule of *contra proferentem* should not be applied in this case because it has been applied generally in ERISA cases only for the purpose of granting benefits under insurance contracts. Microsoft is incorrect. It is true that the rule of *contra proferentem,* which is strictly applied in the interpretation of insurance contracts, is not automatically applied to *all* other contracts. *Eley v. Boeing Co.*, 945 F.2d 276, 280 (9th Cir. 1991). We have declined to apply the rule to "ERISA plans that are the

product of collective bargaining agreements reached after arms-length bargaining between parties of equal power." *Patterson v. Hughes Aircraft Co.*, 11 F.3d 948, 950 n. 3 (9th Cir. 1993); *see Eley*, 945 F.2d at 280 (distinguishing *Kunin* because the plan was the result of a collective bargaining agreement); *see also Kunin*, 910 F.2d at 540. This case does not involve such a plan, and we see no reason to create a new exception to the rule we generally follow in ERISA cases. *See Barnes*, 64 F.3d at 1393.

We have also held that when an administrator has exercised his discretion to construe a plan pursuant to discretionary authority vested in him by the plan, we will not apply the rule of *contra proferentem* in our review of his discretionary ruling. *Winters v. Costco Wholesale Corporation*, 49 F.3d 550, 554 (9th Cir. 1995). Microsoft argues that this case falls within this exception. Clearly, it would be inconsistent to review under an abuse of discretion standard and then to apply the rule of *contra proferentem*. However, as we explained earlier, the administrator did not construe the disputed terms of the plan, and therefore our review is *de novo*. When we review under a *de novo* standard, there is no similar inconsistency, and thus no reason not to apply the rule of *contra proferentem*.

Accordingly, we agree with the magistrate judge, who concluded that Microsoft, "[a]s the drafter of the plan, . . . could easily have accomplished the limitation it now urges through the use of more explicit language. . . ." We therefore construe the ambiguity in the plan against Microsoft and hold that the plaintiffs are eligible to participate under the terms of the SPP. We note that in doing so, we construe the phrase "on the United States payroll of the employer" in the manner we believe to be the most plausible anyway. Put

more directly, were we not to apply the rule of *contra proferentem*, but simply to select the more reasonable of the competing interpretations, we would read the disputed phrase as do the plaintiffs. Thus, we would conclude in any event that the plan must be construed as extending participation to all persons employed by Microsoft and paid from its United State accounts, and not as excluding from participation those employees who are paid through the accounts receivable department rather than the payroll department.

III

The parties agree that the plaintiffs' claims for stock-option benefits under the ESPP are not subject to ERISA but rather are governed by Washington state law. The plaintiffs contend that the ESPP, through its incorporation of § 423 of the Internal Revenue Code, extended eligibility to participate in the plan to all common-law employees, including themselves, and that they were therefore entitled to exercise the options. Microsoft contends that the plaintiffs are not enticed to ESPP benefits because: (1) the plaintiffs have no right to enforce § 423; (2) the plaintiffs signed instruments stating that they would receive no benefits; and (3) the ESPP was never communicated to the plaintiffs, and they therefore did not rely on the offer in continuing their employment. We address these contentions in turn.

First, we hold that the named plaintiffs and the class they represent are covered by the specific provisions of the ESPP. We apply the "objective manifestation theory of contracts," which requires us to "impute an intention corresponding to the reasonable meaning of a person's words and acts." *Multicare Medical Ctr. v. DSHS*, 114

Wash.2d 572, 790 P.2d 124, 133 (1990). Through its incorporation of the tax code provision into the plan, Microsoft manifested an objective intent to make all common-law employees, and hence the plaintiffs, eligible for participation. The ESPP specifically provides:

> It is the intention of the Company to have the Plan qualify as an "employee stock purchase plan" under Section 423 of the Internal Revenue Code of 1954. *The provisions of the Plan shall, accordingly, be construed so as to extend and limit participation in a manner consistent with the requirements of that Section of the Code.*

(Emphasis added). The requirements of § 423 dictate that "options are to be granted to all employees of any corporation whose employees are granted any of such options by reason of their employment by such corporation." 26 U.S.C. § 423(b)(4). Because the term "employees" in § 423 is construed to refer to "common-law employees,"[10] the ESPP, when construed in a manner consistent with the requirements of § 423, extends participation to all common-law employees not covered by one of the express exceptions

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[10] Treasury Regulation § 1.423-1(b) cross-references § 1.421-7(h) for rules relating to the employment relationship. That subsection, in turn, provides that the determination whether an optionee is an employee will be made in accordance with § 3401(c)-1(a), which states that the term "employee" includes every individual performing services for another where the legal relationship between the two is that of employer and employee. Section 31.3401(c)-l(b) summarizes the common-law test of employee, and § 31.3401(c)-1(c) provides that where the legal relationship exists, the labels used by the parties to describe the relationship are of no consequence.

set forth in the plan.[11] Accordingly, we find that the ESPP, through its incorporation of § 423, expressly extends eligibility for participation to the plaintiff class and affords them the same options to acquire stock in the corporation as all other employees.

Microsoft argues that § 423 does not grant the plaintiffs a private right of enforcement. We conclude, as did the magistrate judge, that Microsoft's argument is without merit. This case is not about a private right of action. It is about the construction of the terms of a plan. As the magistrate judge cogently stated,

> Plaintiffs do not contend that § 423, *per se*, provides them with a private right of enforcement. What they *do* contend is that Microsoft expressly incorporated § 423's terms into its ESPP, thereby making an offer to its employees, including its "common law employees," a classification in which they belonged.

Because the plan, properly construed, extends participation to all common-law employees, the plaintiffs may enforce the

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[11] Section 423(b)(4) sets forth four express exceptions. The ESPP incorporates two of them, as follows:

> [a]ny employee of the Company or any of its subsidiaries who is in the employ of the Company at one of the offering dates is eligible to participate in the Plan, except (a) employees whose customary employment is 20 hours or less per week, and (b) employees whose customary employment is for not more than five months in the calendar year.

The plaintiffs fit neither of these exceptions.

plan in the same manner as would any of Microsoft's other employees. They may, and did, assert a cause of action for breach of contract, not for violation of the Internal Revenue Code.[12]

Microsoft next contends that the non-disclosure agreements and the information documents signed by the plaintiffs render them ineligible to participate in the ESPP. First, the label used in the instruments signed by the plaintiffs does not control their employment status.[13] Second,

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[12] A similar approach obtains with respect to plans that require compliance with the provisions of ERISA. While Internal Revenue Code provisions and Treasury regulations do not create substantive rights under ERISA, if an ERISA plan explicitly provides that it is to be construed to meet such provisions, courts look to them in determining employee eligibility for participation in the plan. *See Crouch v. Mo-Kan Iron Workers Welfare Fund*, 740 F.2d 805, 809 (10th Cir. 1984) ("Because the pension plan states that it is to be construed to meet the requirements of ERISA, [the participating and vesting rules require the inclusion of a person in plaintiff's position in the plan,] and there are obvious and significant benefits to meeting those requirements, we conclude that we must construe the plan as including plaintiff as a participant."); *see also Abraham v. Exxon Corp.*, 85 F.3d 1126, 1131 (5th Cir. 1996) (finding that court could not look to Treasury regulations to determine employee eligibility for participation in an ERISA plan when it did not contain an explicit provision "declaring that it was to be construed to meet the requirements of an ERISA plan").

[13] The pertinent Treasury Department regulation provides that

> [i]f the relationship of employer and employee exists, the designation or description of the relationship by the parties as anything other than that of employer and employee is immaterial. Thus, if such relationship exists, it is of no consequence that the employee is designated as

(continued...)

the employment instruments, if construed to exclude the plaintiffs from receiving ESPP benefits, would conflict with the plan's express incorporation of § 423. Although Microsoft may have generally intended to exclude individuals who were in fact independent contractors, it could not, consistent with its express intention to extend participation in the ESPP to all common-law employees, have excluded the plaintiffs. Indeed, such an exclusion would defeat the purpose of including § 423 in the plan, because the exclusion of common-law employees not otherwise excepted would result in the loss of the plan's tax qualification.

Moreover, we find nothing inconsistent between the employment instruments signed by the plaintiffs, and an offer of participation in the ESPP. The statements in those instruments that speak in terms of the employee being "responsible for . . . other benefits" or "responsible to pay all [his] own insurance and benefits" apply most naturally to health and welfare benefits, or similar employee protection policies, which an employee would have to pay on his own if the employer did not provide the benefits. In fact, we find the instruments fully consistent with the plaintiffs' participation in the ESPP, because, under the terms of the plan, it is the employee who makes the stock option payment, not Microsoft. Thus, it *is* the employee who is "responsible" for paying for the benefit. Accordingly, even if the incorporation

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[13] (...continued)

a partner, coadventurer, agent, *independent contractor*, or the like.

Treas. Reg. § 31.3401(c)-1(e) (emphasis added). Accordingly, that the instruments describe the plaintiffs as independent contractors and provide that as such they are not entitled to benefits is not controlling.

of § 423 did not override the instruments signed by the plaintiffs, we would conclude that nothing in those instruments serves to waive or otherwise foreclose the plaintiffs' eligibility for participation in the ESPP.[14]

Finally, Microsoft maintains that the plaintiffs are not entitled to ESPP benefits because the terms of the plan were never communicated to them and they were therefore unaware of its provisions when they performed their employment services. As a preliminary matter, we find Microsoft's reliance on policy manual cases such as *Kimbro v. Atlantic Richfield Company*, 889 F.2d 869, 879 (9th Cir. 1989), to be misplaced. In *Kimbro*, we stated that under Washington precedent, an employer may be contractually bound by promises in employee handbooks or manuals to provide specific treatment in specific situations only if an employee can show that the promise induced his reliance—that is, "that the promise induced him to remain on the job or not seek other employment." 889 F.2d at 879 (quoting *Thompson v. St. Regis Paper Co.*, 102 Wash.2d 219, 685 P.2d 1081, 1088 (1984)). However, many policy manuals are primarily designed for internal guidance and such manuals are far different in nature and legal effect than tax-qualified benefit plans that fix the rights of their beneficiaries.[15]

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[14] For this reason, Microsoft's reliance on *Grimes v. Allied Stores Corporation*, 53 Wash. App. 554, 768 P.2d 528, 529 (1989), in which the court considered a conflict between an employment contract and an employment manual, is inapposite.

[15] Washington case law regarding pension plans, for example, holds that "[a]n enforceable contract will arise . . . even though the [employee] does not know the precise terms of the pension agreement." *Dorward v. ILWU-PMA Pension Plan*, 75 Wash.2d 478, 452 P.2d 258, 260 (1969).

In any event, to the extent that knowledge of an offer of benefits is a prerequisite, it is probably sufficient that Microsoft publicly promulgated the plan. In *Dangott v. ASG Industries, Inc.*, 558 P.2d 379, 382 (Okla. 1976), the plaintiff was unaware of the company's severance plan until shortly before his termination. The Oklahoma Supreme Court concluded nonetheless that publication of the plan was "the equivalent of constructive knowledge on the part of *all* employees not specifically excluded." *Id.* at 383 (emphasis added).[16] Here, the plaintiffs knew of the plan but were wrongly told by Microsoft that it did not apply to them. We are not aware of any Washington case involving a similar set of circumstances, but think it likely that if presented with the question, the Washington Supreme Court would adopt the *Dangott* approach, at least under the circumstances presented in this case.

Microsoft itself recognizes "the key distinction between offers actually made to a class of employees, as to which some courts enforce the offer on behalf of *any* class member, regardless of individual knowledge of the offer, and plans as to which no offer is made to the class, and the class is expressly notified no offer is being made." (Emphasis added). Here, the plan was distributed to Microsoft employees generally. By its terms, the plan extends

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[16] *See Woolley v. Hoffman-LaRoche, Inc.*, 99 N.J. 284, 491 A.2d 1257, 1268 n. 10 (1985) ("The implication of the presumption of reliance is that the . . . provisions became binding the moment the [plan] was distributed. Anyone employed before or after became one of the beneficiaries of those provisions. And if [*Toussaint v. Blue Cross & Blue Shield*, 408 Mich. 579, 292 N.W.2d 880 (1980)] is followed, employees neither had to read it, know of its existence, or rely on it to benefit from its provisions . . . ."); *see also* A. Corbin, *Contracts* § 59 (1963) (suggesting that knowledge of an offer is not necessary to establish acceptance).

participation to the class of common-law employees, and hence offers ESPP benefits to all members of that class.[17] Thus, applying the "key" distinction recognized by Microsoft, an offer was actually made to a class of employees of which the plaintiffs were a part, and it may be enforced on their behalf regardless of their individual knowledge regarding the offer.

We are not required to rely, however, on the *Dangott* analysis or even on Microsoft's own unwitting concession. There is a compelling reason, implicit in some of the preceding discussion, that requires us to reject the company's theory that the plaintiffs' entitlement to ESPP benefits is defeated by their previous lack of knowledge regarding their rights. It is "well established" that an optionor may not rely on an optionee's failure to exercise an option when he has committed any act or failed to perform any duty "calculated to cause the optionee to delay in exercising the right." 17A Am.Jur.2d *Contracts* § 85 (1991 &

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[17] Microsoft contends that despite promulgation of a plan, no rights are created unless a promise is made directly to the affected employees. The two cases cited by Microsoft in support of this proposition, *Estate of Bogley v. United States*, 206 Ct. Ct. 695, 514 F.2d 1027 (1975), and *Schmidt v. Avco*, 15 Ohio App.3d 81, 472 N.E.2d 721, *aff'd*, 15 Ohio St.3d 310, 473 N.E.2d 822 (1984), are readily distinguishable. In *Bogley*, a corporate board of directors voted to offer the plaintiff a severance plan but never actually offered it to him. In *Schmidt*, there was no allegation that the severance pay policy was published or generally distributed to Avco employees. We also reject Microsoft's argument that the plaintiffs represent a separate class. The plaintiff class is a subset of the class of common-law employees as to whom Microsoft failed to honor its promise of benefits. That the plaintiffs were wronged in this manner hardly makes them a separate class for purposes of determining the scope of the promise.

Supp. 1996). "[T]he optionor may not make statements or representations calculated to cause delay, [or] fail to furnish [necessary] information...." *Id.* Similarly, "[I]t is a principle of fundamental justice that if a promisor is himself the cause of the failure of performance, either of an obligation due him or of a condition upon which his own liability depends, he cannot take advantage of the failure." *Highlands Plaza, Inc. v. Viking Investment Corp.*, 72 Wash.2d 865, 435 P.2d 669, 676 (1967) (quoting 5 *Williston on Contracts* § 67 (3d ed. 1961)); *James S. Black & Co. v. P & R Co.*, 12 Wash. App. 533, 530 P.2d 722, 724 (1975) (same); *Refrigeration Eng'g Co. v. McKay*, 4 Wash. App. 963, 486 P.2d 304, 309 (1971) (same); *see Restatement of Contracts* § 295 (1932).

Applying these principles, we agree with the magistrate judge, who concluded that Microsoft, which created a benefit to which the plaintiffs were entitled, could not defend itself by arguing that the plaintiffs were unaware of the benefit, when its own false representations precluded them from gaining that knowledge. Because Microsoft misrepresented both the plaintiffs' actual employment status and their eligibility to participate in the ESPP, it is responsible for their failure to know that they were covered by the terms of the offer. It may not now take advantage of that failure to defeat the plaintiffs' rights to ESPP benefits. Thus, we reject Microsoft's final argument.

CONCLUSION

For the reasons stated, the district court's grant of summary judgment in favor of Microsoft and denial of summary judgment in favor of the plaintiffs is REVERSED and the case REMANDED for the determination of any

questions of individual eligibility for benefits that may remain following issuance of this opinion and for calculation of the damages or benefits due the various class members.

REVERSED and REMANDED.

TROTT, Circuit Judge, Dissenting:

I

The Savings Plus Plan

Microsoft has a *payroll* department, and it has a separate *accounts payable* department. Because these plaintiffs were regarded both by Microsoft *and* by themselves as independent contractors or freelancers, Microsoft did not budget or pay for them through the payroll department, but through the accounts payable department. This commonplace distinction is fatal to the plaintiff request for Savings Plus Plan ("SPP") benefits because to be eligible for these benefits, they have to have been on the employer's "payroll." The Plan itself so states.

As freelancers, the plaintiffs worked for Microsoft with the clear understanding that they were not entitled to the benefits they now seek. They knew Microsoft paid them based on the submission of invoices and out of accounts payable. Nevertheless, they now contend—without a foot to stand on—that they were indeed on Microsoft's "payroll" and thus eligible for SPP benefits. In my reading of this record, they were not on Microsoft's "payroll," period. I agree with the district court's analysis. All this may seem formalistic to the casual reader, but it was an important

distinction to Microsoft, *and* to these workers when they agreed as freelancers to perform work for this company.

How the plaintiffs got on Microsoft's payroll budget from the accounts payable department is a strange tale based not on the facts, but on an immaculate patching together by the majority of a series of interpretations, constructions, presumptions, plausibilities, assertions, and assumptions, topped off by an irrelevant definition of "payroll" in a Random House dictionary. This amalgam is driven in turn by an IRS ruling that the majority takes way beyond its necessary reach. The majority's strained and Urbanesque journey belies its claim that it does not create ambiguity where none exists. In the context of this case—forget Random House—"payroll" has an ascertainable meaning illustrated in large measure by the existence in Microsoft of an alternative method of paying people for their work: out of accounts payable. Anyone familiar with business is familiar with this distinction. Where is the ambiguity but in the eyes of uninitiated outsiders? I discern none, and the plaintiffs saw none either when they voluntarily worked under these circumstances.

As the majority indicates, we interpret terms in ERISA plans "in an ordinary and popular sense as would a person of average intelligence and experience," but we should do so with an eye to what those hypothetical people actually know (e.g., that they did not bargain for the payroll benefits they now seek). To do otherwise is to engage in head-in-the-sand thinking. All the maxims invoked by the majority to support their holdings are useless unless they square with the facts. If I *know* I have a "no benefits" contract, for example, what good does it do to ask what the ordinary average Babbitt (George, not Bruce) might believe after reading a Random

House dictionary? These plaintiffs were university-educated. One had a law degree. They *knew* what they were getting into, and *contra proferentem* should not suggest otherwise. The majority's preference for answering this issue as a theoretical rather than a real question is wrong.

But for the sake of argument, we can ignore the contextual definition of "payroll" and concede the existence of an ambiguity created by the words "United States." Then we can examine extrinsic evidence to see if the plaintiffs have a righteous claim to this benefit. Here, their argument becomes tenuous in the extreme. The plaintiffs have not presented a shred of relevant extrinsic evidence that would justify *their* belief (after signing the documents they did and after accepting the contractual relationship governing this case) that they were on the payroll and entitled to any of the payroll benefits of regular employees, including the SPP. Plaintiff Vizcaino's answers in her deposition testimony, answers representative of the testimony of all plaintiffs, adequately illustrate this point:

> Q. You didn't ask anything [during your initial interview] about the benefits on this job?
>
> A. Well, yeah, I must have I guess. I don't remember what we said but I guess it—yeah, *we weren't going to get benefits at that time.*
>
> Q. Okay. And just so we understand each other, when you say benefits—let me rephrase the question. By benefits I assume that you mean, and correct me if I'm wrong, things like holidays, vacation, sick leave, other kinds of paid leave, participation in the employee stock

purchase plans, that kind of thing. Is that the way you mean benefits?

A. Yeah.

Q. Okay. Now, at the end of this conversation, this interview with Ms. Carter, I assume it was at the end of the conversation, did you accept the position on the terms that had been discussed in that interview?

A. Yes.

(emphasis added). Equally telling is the deposition testimony of plaintiff Culbert:

Q. Did you ever hear anybody use the term "regular employee" during your time at Microsoft when you were a freelancer?

A. I do recall, yes.

Q. And when that term was used did you understand it to refer to *people who were salaried as opposed to freelancers*?

A. Yes.

Q. So that until this status change [when Culbert became a regular employee] in October of 1989 you were never a regular employee at Microsoft?

A. I worked at Microsoft consistently.

Q. But you were never what was referred to as a regular employee?

A. That's correct. I was never what was referred to as a regular employee at that time, correct.

Q. And I take it at no time before October of 1989 did you ever apply for benefits of any type from Microsoft: sick leave, vacation, holidays, participation in the employee stock purchase program?

A. I didn't apply for those things.

* * * *

Q. But during the course of the next few weeks or months [after beginning work at Microsoft] it became clear to you that being a freelancer meant that you got no benefits?

A. That it meant something, if I may, it meant that in some ways *I was different from the regular salaried employees with whom I worked.*

Q. But *among those ways of which it made [sic] you different was that you got no benefits?*

A. Correct.

(emphasis added). In the light of this testimony, this case becomes just another example of litigants trying to force their feet into glass slippers that do not fit. As the

magistrate judge correctly observed, these plaintiffs had express contracts for "no benefits."

Why they would accept such an arrangement *without* benefits is also clear from the record: Microsoft paid them more *cash* on an hourly basis than regular employees. Plaintiff Culbert explains:

> Q. Did you have any understanding at that time [when you became a regular employee of Microsoft] about whether it was common for freelancers to be making more on an hourly basis than the equivalent hourly rate for people who were regular salaried employees?
>
> A. Yes.
>
> Q. What was your understanding?
>
> A. That in general freelance production editor [sic] on a gross cash basis would stand to make more than a regular staff employee.

Nevertheless, the plaintiffs brought this lawsuit pursuing not only SPP and stock purchase benefits, but vacation, sick leave, holidays, short-term disability, and group health and life insurance as well, i.e., the best of both worlds.

With all respect to my colleagues, their atmospheric use of the IRS's determination to shore up their analysis by suggesting Microsoft is a tax cheat is gratuitous and inappropriate. I do not discern on the part of Microsoft an unlawful purpose to violate the tax laws. What the IRS does for the purpose of collecting its due—both early and from

the most reliable pocket—need not cast a dark light on a relationship with which both Microsoft and these employees were comfortable. It simply does not follow either from the IRS's ruling or from Microsoft's compliance with it (1) that these plaintiffs were *payroll* employees *or* (2) that to deny the plaintiffs' claim gives Microsoft unacceptably unclean hands. To quote the United States General Accounting Office in June of 1996,

> [M]any employers struggle in making the [employee/independent contractor] classification decision because of the unclear rules. Until the classification rules are clarified, we are not optimistic that the confusion over who is an independent contractor and who is an employee can be avoided. The Treasury Department characterized the situation in 1991 in the same terms as it used in 1982; namely, that "applying the [20 factor] common law test in employment tax issues does not yield clear, consistent, or satisfactory answers, and reasonable persons may differ as to the correct classification."[1]

As the magistrate judge observed, "[p]laintiffs concede that the IRS ruling . . . is in no way binding on this court." The IRS's familiar aggressive tax collection position and

---

[1] General Accounting Office, Pub. No. GAO/T-GGD-96-130, *Tax Administration: Issues in Classifying Workers as Employees or Independent Contractors* 5 (1996) (statement of Natwar M. Gandhi, Associate Director, Tax Policy and Administration Issues, General Government Division).

Microsoft's payroll argument can exist independently of each other without doing violence to the law.[2]

By tone and by choice of words the majority seems subtly to accuse Microsoft of reprehensible conduct towards its workers. Microsoft is identified as "refusing" to pay its workers fringe benefits as though it did something wrong in creating the contractual relationships in this case. Later in the opinion the majority charges Microsoft with "misrepresenting" to the plaintiffs their employment status and with taking advantage of them. They clothe Microsoft with a Dickensian anti-labor attitude. Such characterizations spring full-bloom from the first sentence of the majority's opinion where "avoiding payment of employee benefits" and "increasing profits" foreshadow the negative coloration of the infidel Microsoft's role in this drama. The majority's tone and accusations go against the factual record as developed and described by the magistrate judge in his Report and Recommendation dated April 15, 1994:

> Plaintiffs offer the explanation that Microsoft really knew all along that they were regular "employees" entitled to benefits, and hid this entitlement from them by "mislabeling" them as independent contractors or freelancers. *This argument is not persuasive.* "Mislabeling" as used by Plaintiffs implies a unilateral act by Microsoft which in some

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[2] Because independent contractors have been found by the IRS to have a lower compliance rate than employees in paying their taxes—to the tune of two to three *billion* dollars a year—the IRS adopted an aggressive enforcement program in 1986 resulting to date in 12,983 Employment Tax Examination Program audits and the reclassification of 527,000 workers. *Id.*

> way hid their true status from Plaintiffs. *In truth, Microsoft was quite open about the terms of its working relationships with Plaintiffs on the subject of employee benefits* and *each of the Plaintiffs fully understood and accepted those terms.*

(emphasis added).

Neither federal nor state law mandates the benefits sought, nor does the applicable collective bargaining agreement. Microsoft was free to offer the benefits in return for work as Microsoft saw fit. Thus, the majority seems to overlook the constitutional right of private parties freely to enter into contracts of their own choice and benefit. It is not for the courts under these circumstances to add clauses to agreements that the parties never contemplated, or to accuse parties of attitudes and behavior of which they are not guilty. Congress designed ERISA to protect benefits workers already had, not to give them benefits for which they did not contract. *See* 18 U.S.C. § 1001 (Congressional findings and declaration of policy).

II

The Employee Stock Purchase Plan

The plaintiffs' second claim of entitlement is to stock option benefits under Microsoft's Employee Stock Purchase Plan ("ESPP"), a claim we process under the law of the State of Washington. The law in question is the Washington law of *contracts.*

As with the plaintiffs' first claim, the majority engages in analytical gymnastics to find a contractual right where

none exists. No one disputes that the offer made by Microsoft and accepted by the plaintiffs explicitly excluded the ESPP benefits now sought. Plaintiffs freely admit as demonstrated earlier that they never expected when these contracts were formed to receive any such benefits. Microsoft never offered the benefits to the plaintiffs, either bilaterally or unilaterally, the plaintiffs never accepted them, and the plaintiffs never relied on them in any way whatsoever as part of their compensation package. As the magistrate judge found in his Report and Recommendation,

> Microsoft indeed offered such benefits to its "regular employees" and described them in employee handbooks issued to regular employees, but not to freelancers. Moreover, it is not contended by any Plaintiff that he/she was ever offered such benefits by any Microsoft spokesperson, or even a handbook, and to the extent that any of them saw the books, they understood that they were *not entitled* to them.

Thus, without an offer, without acceptance, without consideration, and without a meeting of the minds, the majority creates by operation of law a contractual right on behalf of these plaintiffs that they never even contemplated until this lawsuit began.

This unpredictable result is so radical that it trespasses on Article I, section 10, Clause 1 of the Constitution, which prohibits a state from impairing the obligation of contracts. Neither through legislation nor by judicial act could a state severely transmogrify a contractual obligation in this manner and force one party to it to confer such benefits on the other. The result in this case resembles the thrust of the

Minnesota statute struck down by the Supreme Court in *Allied Structural Steel Co. v. Spannaus*, 438 U.S. 234, 98 S.Ct. 2716, 57 L.Ed.2d 727 (1978). In that case, Minnesota had enacted a law requiring certain private employers who provided pension benefits under a plan meeting the qualifications of section 401 of the Internal Revenue Code to provide pension benefits "conspicuously beyond those that [the company] had voluntarily agreed to undertake." *Id.* at 240, 98 S.Ct. at 2720. The Supreme Court held this statute unconstitutional under the contracts clause (1) because it failed to deal with a "broad, generalized economic or social problem," and (2) because of its narrow aim at only certain employers. The Court noted also in the employer's favor (1) that the employees of Allied Structural never relied on the statutory benefit at issue, and (2) that the statute "compelled the employer to exceed bargained-for expectations and nullified an express term of the pension plan." *Id.* at 246 n. 18, 98 S.Ct. at 2723 n. 18. Justice Stewart said,

> The severity of an impairment of contractual obligations can be measured by the factors that reflect the high value the framers placed on the protection of private contracts. Contracts enable individuals to order their personal and business affairs according to their particular needs and interests. Once arranged, those rights and obligations are binding under the law, and the parties are entitled to rely on them.

Id. at 245, 98 S.Ct. at 2723.[3] Because we are bound to apply state law to this dispute, we have no authority to impair the obligation of these contracts either. To do so is tantamount to depriving Microsoft of property without due process of law.

CONCLUSION

The IRS's understandably tough enforcement program not only collects more money for the government, but it now has the unforeseen and unnecessary consequence of forcing employers retroactively to extend to workers optional benefits for which they did not contract. I perceive no need whatsoever to permit the IRS's ruling to spill out of its unique context and to do damage to contracts between companies and workers. The ruling and the contracts can exist independently of each other. Peaceful coexistence simply means that all workers will be made to pay their taxes, no more, no less, and that all workers will get that for which they bargained. Thus, I respectfully dissent.

---

[3] *See also Associated Builders & Contractors, Golden Gate Chapter v. Baca*, 769 F. Supp. 1537 (N.D. Cal. 1991) (holding that municipal legislation requiring contractors to pay minimum wages and benefits in order to receive private building permits unconstitutionally impaired the contractors' collective bargaining contracts).

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On Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

MOTION FOR LEAVE TO FILE BRIEF *AMICI CURIAE* AND BRIEF *AMICI CURIAE* OF INFORMATION TECHNOLOGY ASSOCIATION OF AMERICA, AMERICAN STAFFING ASSOCIATION, ASSOCIATION OF PRIVATE PENSION AND WELFARE PLANS, AND NATIONAL TECHNICAL SERVICES ASSOCIATION IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI OF MICROSOFT CORPORATION

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MOTION FOR LEAVE TO FILE BRIEF *AMICI CURIAE*

Information Technology Association of America, American Staffing Association, Association of Private Pension and Welfare Plans, and National Technical Services Association (collectively the "Employer Amici") respectfully move this Court, pursuant to Supreme Court Rule 37, to grant leave to file their brief, submitted herewith, as *Amici Curiae* in support of the Petition for Writ of Certiorari filed by Microsoft Corporation ("Microsoft").

Pursuant to Supreme Court Rule 37.2, the Employer Amici have obtained the consent of Petitioner Microsoft Corporation to the filing of their Brief *Amici Curiae*. However, Stephen Strong, Counsel for Respondents Donna Vizcaino, *et al.*, declined to consent to the filing of this Brief.

The Employer Amici are the leading trade associations in the information technology ("IT"), flexible staffing

and employee benefits fields. Information Technology Association of America ("ITAA") is a leading trade association of the companies that create and market products and services associated with computers, communications and data. ITAA's 11,000 direct and affiliate members encompass systems integration, professional services, telecommunications, Internet, electronic commerce, client-servers and custom software manufacturing. The IT industry's workforce currently totals over 2.5 million individuals, ten times that of the basic steel industry, and three times that of the automotive industry. IT is our country's number one export.

American Staffing Association ("ASA") is an industry association of firms that supply temporary help and other staffing services to businesses around the world. ASA is the nation's largest association of staffing supply firms. ASA members operate over 13,000 staffing offices, representing almost 75% of the staffing firm offices in the United States. Collectively, the staffing industry had approximately $60 billion in domestic temporary help revenue in 1998. It currently employs almost 3 million people in the United States on a daily basis and an estimated 15 million annually.

Association of Private Pension and Welfare Plans ("APPWP") is a broad-based, non-profit trade association which was founded in 1967 to protect and foster the growth of the private employer-sponsored employee benefit plan system in the United States. Its members include both small and large employer sponsors of employee benefit plans, as well as numerous plan support organizations, such as consulting and actuarial firms, investment firms, banks, insurers and other professional organizations. Collectively, it has more than 230 members who sponsor or administer plans covering more than 100 million plan participants.

National Technical Services Association ("NTSA") is comprised of companies that contract out their employees —qualified designers, drafters, engineers, computer programmers, systems analysts and other experienced professional technical personnel—to public and private businesses. Serving leading edge companies in a variety of industries such as IT, electronics, telecommunications, aerospace, biotechnology, pharmacology and financial services, NTSA member firms operate over 1,800 offices and employ more than 300,000 technical professionals nationwide and around the globe.

Flexible staffing arrangements play a vital role in American industry today. Businesses rely on flexible staffing arrangements to fill positions while employees are on leave, meet staffing needs during temporary growth spurts, or staff short-term projects that require specialized skills that their employees lack.

Flexible staffing is particularly common in the IT industry, where skilled workers may be brought into a business to address Y2K compliance, build or service computer networks or assist in developing software. Businesses will frequently turn to IT staffing firms because they lack the technical ability to evaluate or supervise IT workers. If a project has a limited time line or the client does not have sufficient work to keep skilled workers busy for the foreseeable future, flexible staffing firms may be the *only* practical source of personnel to accomplish the needed tasks.

Positions filled by staffing firm workers may last from a few days to more than a year. In some cases the client may supervise the details of the work—for example, when staffing firm employees perform clerical or administrative work. In other cases, however, particularly in IT fields, the staffing firm employee has a level of exper-

tise that precludes the client from supervising the details of the work performed. Nevertheless, even when the IT staffing firm "directs" a specific project, it may still be necessary for the client to coordinate when, where and how staffing firm employees are permitted to access the client's IT systems, in order to maintain the integrity and security of the client's records and assure that the staffing firm's work does not interfere with the client's ability to conduct business.

In May 1999, the Ninth Circuit ruled in *Vizcaino v. Microsoft Corp.*, 173 F.3d 713 (9th Cir. 1999) ("*Vizcaino III*"), that individuals performing services for a business through a staffing firm may be employees of *both* the staffing firm and the business that contracted for their services. Completely unprecedented in the employee benefits context, this "dual employer" status created by the Ninth Circuit exposes businesses that use staffing firm employees to lawsuits for retroactive employee benefit coverage by staffing firm employees who may already be receiving employee benefits from their staffing firms. The "dual employer" analysis is also entirely unworkable under the Internal Revenue Code.

Because of their role as the leading trade associations for industries that use or supply flexible staffing, the Amici have an understanding of the impact the *Vizcaino III* decision will have on these industries nationwide. The Amici's Brief sets forth the critical role that alternative workers play in the IT industry and the United States as a whole. It explains, from the Amici's unique perspective, the significant, adverse impact the newly created dual employer status will have on the businesses that provide flexible staffing services and on the industry segments that are significant consumers of staffing services.

The Brief, which consolidates the views of four leading trade associations troubled by the Ninth Circuit's decision,

also flushes out the deficiencies in the Ninth Circuit's substantive analysis of the plaintiffs' employment status for employee benefit purposes, revealing its conflict with Internal Revenue Code provisions enacted by Congress. The Employer Amici believe that their Brief will impress upon the Court the importance of this case to flexible staffing firms, and to United States employers generally, and the critical need for this Court to grant Microsoft's Petition for Writ of Certiorari.

This motion is timely filed pursuant to Supreme Court Rule 37.2.

For the foregoing reasons, the Employer Amici respectfully request that the Court grant them leave to file their Brief *Amici Curiae* in support of Microsoft's Petition for Writ of Certiorari.

Respectfully submitted,

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INTEREST OF THE *AMICI CURIAE*

Information Technology Association of America, American Staffing Association, Association of Private Pension and Welfare Plans, and National Technical Services Association (collectively the "Employer Amici") respectfully submit this Brief *Amici Curiae* [1] in support of the Petition for Writ of Certiorari filed by Microsoft Corporation ("Microsoft").

[1] This brief was authored in whole by counsel for the Employer Amici, Seyfarth, Shaw, Fairweather & Geraldson.

Information Technology Association of America ("ITAA") is a leading trade association of the companies that create and market products and services associated with computers, communications and data. ITAA's 11,000 direct and affiliate members encompass systems integration, professional services, telecommunications, Internet, electronic commerce, client-servers and custom software manufacturing. The information technology ("IT") industry's workforce currently totals over 2.5 million individuals, ten times that of the basic steel industry, and three times that of the automotive industry. IT is our country's number one export.

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Flexible staffing arrangements play a vital role in American industry today. When businesses need to fill positions while employees are on leave, meet staffing needs during temporary growth spurts, or staff projects that require specialized skills that the businesses' employees lack, staffing arrangements provide them with the necessary manpower to keep their organizations efficient and profitable.

Flexible staffing is particularly common in the IT industry, where skilled workers may be brought into a business to address Y2K compliance, build or service computer networks or assist in developing software. If a project has a limited time line or the client does not have sufficient work to keep skilled workers busy for the foreseeable future, staffing firms may be the *only* practical source of personnel to accomplish the needed tasks.

Positions filled by staffing firm workers may last from a few days to more than a year. In some cases the client may oversee the details of the work—for example, when staffing firm employees perform clerical or administrative work. In other cases, however, particularly in IT fields, the staffing firm employee has a level of expertise that precludes the client from supervising the details of the work performed. Nevertheless, even when the IT staffing

firm "directs" a specific project, it may still be necessary for the client to coordinate when, where and how staffing firm employees are permitted to access the client's IT systems, in order to maintain the integrity and security of the client's records and assure that the staffing firm's work does not interfere with the client's ability to conduct business.

The decision of the Ninth Circuit in *Vizcaino v. Microsoft Corp.*, 173 F.3d 713 (9th Cir. 1999) (the "Opinion" or "*Vizcaino III*"), if left standing, would make many staffing firm employees the "joint employees" of both the staffing firm and its clients for employee benefit purposes. This newly-created "dual employment" doctrine will expose businesses that use staffing firm employees to lawsuits for employee benefits brought by staffing firm employees who may already be receiving employee benefits from their staffing firm. It will also fundamentally undermine how the employee benefit provisions of the Internal Revenue Code apply to staffing firms and their clients.

SUMMARY OF ARGUMENTS

The Ninth Circuit's ruling in *Vizcaino III* is the first court decision to hold that an individual performing a single job for a single compensation package may be considered to be employed by two unrelated employers for purposes of the employee benefit provisions of the Internal Revenue Code, 26 U.S.C. §§ 401-424 ("Code"). This holding, if left standing, would destroy the legal standards and guidelines on which United States businesses have heretofore based their flexible staffing arrangements. As a result, the Opinion exposes the thousands of businesses that use staffing firm employees for legitimate business reasons to lawsuits for retroactive employee benefit coverage by plaintiffs looking for a windfall.

The Ninth Circuit's "dual employer" analysis is directly contrary to the design of the employee benefit provisions of the Code and to the Congressional intent underlying these provisions. The Opinion effectively repeals the carefully considered provisions of the Code relating to employee leasing and fundamentally undermines the limitations in the Code governing tax-qualified retirement plans.

The Employer Amici urge the Court to grant certiorari to prevent the disruption of a substantial business sector of the U.S. economy and to preserve the integrity of the Code provisions governing employee benefits.

ARGUMENTS

I. THE OPINION CREATES A CAUSE OF ACTION FOR STAFFING FIRM WORKERS TO SEEK WINDFALL, DUPLICATIVE EMPLOYEE BENEFIT COVERAGE.

The Ninth Circuit's ruling in *Vizcaino III* is the first court decision to hold that an individual performing a single job for a single compensation package may be employed by two unrelated employers for purposes of the employee benefit provisions of the Code. Relying upon this Court's application of common law agency principles in *Nationwide Mutual Insurance Co. v. Darden*, 503 U.S. 318 (1982), the Ninth Circuit held that

> even if for some purposes a worker is considered an employee of the agency, that would not preclude his status of common-law employee of Microsoft. The two are not mutually exclusive.

Vizcaino III, 173 F.3d at 723. The *Darden* Court, however, was careful to determine that applying "traditional agency law principles would [not] thwart the congressional design or lead to absurd results" under the applicable statute. *Darden*, 503 U.S. at 323. The Ninth Circuit's cre-

ation of a "dual employer" status under the employee benefit provisions of the Code does exactly that.

Many employees of flexible staffing firms receive employee benefits from the staffing firms which employ them. For example, the Bureau of Labor Statistics has estimated that 57.9% of full-time workers provided by contract firms (staffing firms that typically provide technical services to their customers) have employer-provided health insurance; and 54.9% of such workers are offered employer-sponsored retirement plans. Bureau of Labor Statistics, U.S. Department of Labor, News Release, U.S.D.L. 90-422, *Contingent and Alternative Employment Arrangements, February, 1997, Labor Force Statistics from the Current Population Survey (December 2, 1997).*[2]

By holding that staffing firm employees may simultaneously be employees of the staffing firm and the client firm for employee benefit purposes, the Ninth Circuit permits such employees to recover benefits from *both* of the "dual employers" with respect to the same compensation stream, or to pick and choose their employee benefits from among the array of plans offered by each. The Opinion exposes the thousands of businesses that use staffing firm employees for legitimate business reasons to lawsuits for retroactive employee benefit coverage by plaintiffs looking for a windfall.

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[2] In fact, Code Section 414(n), 26 U.S.C. § 414(n), provides a significant incentive for staffing firms to provide retirement plan benefits, by allowing leased employees in certain "safe harbor" pension plans to be excluded from consideration in testing the client's retirement plans for compliance with Code requirements.

II. THE OPINION IS DIRECTLY CONTRARY TO THE DESIGN OF THE EMPLOYEE BENEFIT PROVISIONS OF THE CODE AND TO CONGRESSIONAL INTENT.

Congress has explicitly, and repeatedly, addressed flexible staffing and leased employee arrangements for employee benefit purposes in Section 414 of the Code.[3] Yet the Ninth Circuit's "dual employer" analysis ignores both the statutory framework and the case law interpreting it. By ignoring the impact of the triangular relationship between staffing firm, employee and client, *Vizcaino III* applies a bludgeon to staffing and leased employee arrangements where Congress chose to use a scalpel.[4] As a result, the court has done enormous damage to the federal tax laws governing employee benefits.

Section 414(n) of the Code governs the treatment of leased employees for purposes of most tax-favored employee benefit plans, including qualified retirement plans, life and health insurance and employee fringe benefits. Under Section 414(n), a "leased employee" is defined as "any person who is not an employee of the recipient and who provides services to the recipient," if (1) the worker has performed services for the recipient on a substantially

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3 The Opinion purports to apply a common law definition of employment status to an employee stock purchase plan governed by Section 423 of the Code. Because other provisions governing employee benefits in the same part of the Code similarly look to common law to determine employment status, the Opinion will have an extraordinarily broad application. *See* 26 U.S.C. §§ 401-424.

4 As discussed in the text, Congress was well aware of the complex issues relating to employee staffing arrangements and addressed them explicitly in Section 414(n) of the Code. In addition, Congress authorized the Secretary of the Treasury to prescribe regulations necessary to prevent the avoidance of employee benefit requirements "through the use of—(1) separate organizations, (2) employee leasing or (3) other arrangements." 26 U.S.C. § 414(o).

full-time basis for at least one year,[5] and (2) the services are performed "under primary direction or control" of the service recipient. 26 U.S.C. § 414(n)(2), *as amended by* Small Business Job Protection Act of 1996, Pub. L. No. 104-188, § 1454, 110 Stat. 1755, 1817 (1996). An individual who is treated as a leased employee under Section 414(n) must be treated as the employee of the service recipient for specified employee benefit testing purposes. 26 U.S.C. § 414(n)(2). However, other than for these specified testing purposes, Section 414(n) contemplates that a leased employee remains an employee of the leasing organization (and not of the service recipient), and does not require that a leased employee be permitted to participate in the service recipient's employee benefit plans. I.R.S. Notice 84-11, Q&A-14, 1984-2 C.B. 469, 471.

The Opinion renders Section 414(n) of the Code a nullity. On its face, Section 414(n)(2) does not apply to an individual who is the common law employee of the service recipient. *Burrey v. Pacific Gas & Elec. Co.*, 159 F.3d 388 (9th Cir. 1998). At the same time, it defines a leased employee as an individual "under primary direction or control" of the service reciepent—a circumstance that under the Ninth Circuit's "dual employer" analysis would necessarily make the individual the employee of the service recipient.[6] If the "dual employer" analysis

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[5] In contrast, the Ninth Circuit's "dual employer" analysis would appear to apply from the first day worked by a staffing firm employee.

[6] Specifically, the Court held:

> In a series of letters, the IRS advised Microsoft that ". . . It is our conclusion that Microsoft either exercised, or retained the right to exercise, direction over the services performed. This control establishes an employer-employee relationship." *Vizcaino I*, 97 F.3d at 1190 n.2. The IRS determinations allow

were the law, there could be no occasion on which an individual would ever be both subject to the service recipient's "primary direction or control," and also not an employee of the service recipient. Thus, the Ninth Circuit's analysis judicially repeals Section 414(n).

The Ninth Circuit not only failed to consider the impact of its "dual employer" concept on the statute affected, it directly contravened the Congressional intent underlying the statute. Congress adopted the current "primary direction or control" standard in Section 414(n)(2) of the Code as part of the Small Business Job Protection Act of 1996, P.L. 104-188, § 1454(a), 110 Stat. 1755, 1817 (1996). The legislative history to this provision makes it clear that Congress rejected the very presumption of employment status based solely on control that the Ninth Circuit adopted:

> The fact that a person is or is not found to perform services under primary direction or control of the recipient for purposes of the employee leasing rules is not determinative of whether the person is or is not a common-law employee of the recipient.

S. Rep. No. 104-281, at 93 (1996), *reprinted in* 1996 U.S.C.C.A.N. 1474, 1567.

Rather, Congress assumed, correctly, that a worker supplied by a staffing firm may, under common law, be the employee of the staffing firm, *and not that of the service recipient*, notwithstanding that the service recipient controls the worker's performance:

> For example, an individual who works under the direct supervision of the service recipient would be

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no exception for individuals in these positions on the grounds that they may be on the payroll of employment agencies. *Vizcaino III*, 173 F.3d at 724.

> considered to be subject to primary direction or control of the service recipient even if another company hired and trained the individual, had the ultimate (but unexercised) legal right to control the individual, paid his wages, withheld his employment and income taxes, and had the exclusive right to fire him. *Thus, for example, temporary secretaries, receptionists, word processing personnel and similar office personnel who are subject to the day-to-day control of the employer in essentially the same manner as a common-law employee are treated as leased employees if the period of service threshold is reached.*

S. Rep. No. 104-281, at 93-94 (1996), *reprinted in* 1996 U.S.C.C.A.N. 1474, 1567-1568 (emphasis added).

The Opinion also undermines other Code provisions that expressly limit the amount of tax-favored employee benefits an employee may receive under an employer's retirement plan. For example, Section 401(a)(17) of the Code limits the amount of an employee's compensation that may be taken into account for purposes of a qualified retirement plan in any year. *See* 26 U.S.C. § 401 (a)(17). For 1999, this limit is $160,000. Because this limitation does not require the aggregation of benefits provided by *unrelated* employers' retirement plans, Treas. Reg. § 1.401(a)(17)-1(c)(3), the Ninth Circuit's ruling will permit a highly paid employee to receive duplicate benefits, on the same $160,000 of compensation, simply by covering the employee in both a staffing firm plan and a client plan. The overall limitation on qualified retirement plan benefits in Section 415 of the Code, as well as the allocation of employer deductions, can be similarly manipulated under the Ninth Circuit's analysis. *See* 26 U.S.C. §§ 404 and 415. Such manipulation would not be possible if the employee at issue was the employee of *either* the leasing organization *or* the client receiving the services, rather than the employee of both.

In *Packard v. Commissioner*, 63 T.C. 621 (1975), the United States Tax Court specifically rejected the argument that individuals covered by a qualified retirement plan could be employed by both a corporation and a related partnership, based on the potential for abuse:

> We do not believe recognition of such a dual capacity is logical, particularly from a tax accounting standpoint. . . . We can only wonder whether if the partnership had attempted to cover these employees under its profit-sharing plan the respondent [IRS] would have permitted the partnership to deduct its contributions in their behalf if all other circumstances were the same.

Id. at 632. As demonstrated above, the Tax Court's concern regarding the impact of dual employment status on the integrity of the Code provisions governing employee benefits is well founded.

By determining that staffing firm employees may be joint employees of a staffing firm and its clients for employee benefit purposes, without taking into account the real legal and economic significance of the flexible staffing relationship or the legislative intent underlying the affected statutory provisions, the Ninth Circuit's ruling in *Vizcaino III* creates a new test of common law employment for employee benefit purposes that dramatically and adversely affects firms that place flexible staffing employees and the firms that utilize them.

CONCLUSION

For the reasons set forth above, we respectfully urge this Court to grant Microsoft's Petition for Writ of Certiorari.

Respectfully submitted,

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No. 99-498

In The

Supreme Court of the United States

MICROSOFT CORPORATION, *et al.*,

Petitioners,

vs.

DONNA VIZCAINO, *et al.*,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

RESPONDENTS' BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

In 1996 and 1997, the Ninth Circuit ruled twice, by a panel and *en banc*, on the construction and enforcement under Washington State law of Microsoft's employee stock purchase plan (ESPP), a discount-price stock purchase plan under IRC § 423 (not an ERISA plan). The Ninth Circuit determined, with respect to a certified class of common-law employees of Microsoft, that they were wrongly excluded from the ESPP. It held that, under the Washington common law of contracts, all common-law employees of Microsoft should be allowed to purchase shares at a discount, despite being required by Microsoft to sign forms incorrectly stating they were not eligible. *Vizcaino I*, 96 F.3d 1187 (9th Cir. 1996) (panel); *Vizcaino II*, 120 F.3d 1006 (9th Cir. 1997) (*en banc*). Microsoft previously sought review by this Court of the merits of the Washington law issues, saying these *Vizcaino I* and *II* decisions were contrary to Washington law. This Court denied certiorari. 118 S.Ct. 899 (1998).

Following remand, the district court, acting *sua sponte*, substantially decertified the class by reducing it to a tiny "sliver" of the former class, *i.e.*, those hired before April 1, 1990. The district court ruled that thousands of other common-law employees of Microsoft who were within the original *stipulated* class definition, and who were eligible to participate in the ESPP under the Ninth Circuit's 1996-97 decisions, now had to *individually* pursue their identical ESPP claims, either by mass interventions in this case or by separate actions.

QUESTIONS PRESENTED – Continued

Upon a petition for mandamus, the Ninth Circuit reversed and enforced its prior mandate, ruling that the district court's substantial decertification of the class after the class prevailed on the merits was contrary to the Ninth Circuit's mandate and contrary to Rule 23(c)(1). *Vizcaino III*, 173 F.3d 713 (9th Cir. 1999). Microsoft again sought rehearing *en banc* by the Ninth Circuit. This time, rehearing was denied without a single vote for rehearing. *Not even the dissenters from the 1996-97 Ninth Circuit decisions on the merits voted for rehearing.* 184 F.3d 1070. Microsoft now petitions for certiorari a second time.

This case does not involve any split in the circuits, any substantive issue of federal law, or any new principles of law. Microsoft simply contends the Ninth Circuit *misapplied* certain well-established procedures and that it misunderstood its own prior decisions on Washington contract law. Thus, the questions presented here are these:

Whether this Court should review Microsoft's argument that the court of appeals misunderstood the scope of its own prior mandate and its own prior decisions on matters of Washington State law – issues which this Court previously declined to review on the merits – and thus whether the court of appeals abused its discretion in enforcing the prior mandate by way of mandamus rather than waiting for another appeal.

Whether, even if the court of appeals misinterpreted its mandate and its own prior decisions on the merits of Washington State law issues, this Court should review

QUESTIONS PRESENTED – Continued

Microsoft's argument that the court of appeals also abused its discretion in holding that the district court erred in its *sua sponte* drastic reduction of the class to a "sliver" of its former size, where this would result in *thousands* of identical claims on the same issues of Washington law resolved in the Ninth Circuit's prior decisions, and in ruling that the district court should not have altered the class definition after the appellate "decision on the merits" under Rule 23(c)(1).

Whether this Court should review Microsoft's argument that the court of appeals erred in reiterating its previous mandate under principles of Washington State common law pursuant to *Erie Railroad v. Tompkins* and Microsoft's argument that the court of appeals should instead have created and applied some sort of federal common law to override Washington common law, to somehow provide in advance for "orderly resolution" of unspecified, possibly similar, arguments in two pending federal district court ERISA cases in Los Angeles and New York.[1]

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[1] These two cases are cited in the Pet., p. 4 and n. 2.

LIST OF PARTIES

The petition lists the named parties. In addition, in 1993 the parties agreed to, and the district court certified, a class. Pet. A89, n. 1. The plaintiffs and members of the court-certified class are collectively referred to herein as the "Workers" (A48-A49).

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RESPONDENTS' BRIEF IN OPPOSITION

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The Ninth Circuit's opinions are reported at 97 F.3d 1187 (9th Cir. 1996) (Pet. A86), *on rehearing*, 120 F.3d 1006 (9th Cir. 1997) (*en banc*) (Pet. A47), *cert. denied*, 118 S.Ct. 899 (1998), *enforced by mandamus*, 173 F.3d 713 (A4), *amended and rehearing en banc denied*, 184 F.3d 1070 (9th Cir. 1999) (A1).

There were also two pertinent district court orders which are not in the petition's appendix. On Dec. 4, 1998, the district court, Judge John C. Coughenour, ordered that individuals who were formerly, but no longer, class members because of the class reduction orders of Judge Carolyn Dimmick (Pet. A25, A33) could *individually* intervene in this case, raising the prospect of this case having *over one thousand individual plaintiffs* instead of simply continuing as a class action. Petition, p. 10 n. 6. Similarly, Microsoft relies (Pet. 11 and n. 8) on one sentence from a partial *dissenting opinion* in *Vizcaino II* at 1018-19 (Pet. A75), for an argument that *Vizcaino III* was wrong. The district court explicitly and correctly rejected Microsoft's previous argument that this statement in a *dissent* was part of the mandate. CR 307, Order (by Judge Dimmick), 1998 WL 122084 at 2-4.

RULE INVOLVED

Rule 23(c)(1), FRCP, states:

> As soon as practicable after the commencement of an action brought as a class action, the

court shall determine by order whether it is to be so maintained. An order under this subsection may be conditional, and may be altered or amended before the decision on the merits.

STATEMENT OF THE CASE

Microsoft's discussion of the facts and the proceedings below is replete with errors and statements of fact with *no* basis in the record. For example, Microsoft contends it neither agreed to the scope of the class here nor did it agree that the class members "generally were common law employees of Microsoft" (Pet., p. 14 and n. 9; see also pp. 16-18), despite numerous judicial findings to the contrary.[2] Microsoft contends that the Ninth Circuit misstated Microsoft's various concessions in 1993-94 on those matters (Pet., p. 14, n. 8) and that "the Magistrate Judge's finding was *rejected* by the District Court prior to the appeal that resulted in the *Vizcaino I* decision" (*id.*, emphasis by Microsoft). In fact, the district court *did not* reject the magistrate judge's finding since *this matter was never presented to the district court by Microsoft* because *Microsoft expressly agreed* to the magistrate judge's findings.[3] The district court later specifically found that

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[2] *Vizcaino I* at 1190 n. 1 (p. A89 n. 1); 1193 n. 4 (p. A96 n. 4); 1195 n. 9 (p. A101 n. 9): *Vizcaino II* at 1010 (p. A53); 1010 (p. A54); 1011 (p. A57); 1012 (p. A58); 1013 (p. A61); *Vizcaino III* at 720 (p. A13, A14).

[3] The magistrate judge said (CR 187 at 34):

Microsoft does not really contend at this point that Plaintiffs were not "common law employees," as

(Continued on next page)

Microsoft had conceded these points. 1998 WL 122084 at 3.[4] Thus, the Ninth Circuit said "Microsoft's

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> found by the IRS for tax purposes, and such a contention, were it to be made, would fly in the face of all of the material facts concerning Plaintiffs' work at Microsoft, the existence of which Microsoft acknowledges.

Microsoft limited its objection to the magistrate judge's recommendation as follows (CR 195 at 2):

> This objection rests on one simple basis. The Plaintiffs' claim for ESPP participation is governed by state contract law. And there was never a contract, express or implied, between Microsoft and the Plaintiffs that entitled them to ESPP participation. . . .
>
> > *Defendants do not object to the factual findings embodied in the Report and Recommendation.* (Emphasis added.)

Under FRCP 72(b), a party's "failure to object to a magistrate's findings of fact waives the right to contest those findings on appeal." *Britt v. Simi Valley Unified School Dist.*, 708 F.2d 452, 454 (9th Cir. 1983).

[4] The district court found (1998 WL 122084 at 3):

> It is clear that Microsoft conceded that "plaintiffs" were common law employees at a number of stages in this case, beginning in 1994, on its motion for summary judgment on the SPP. See Doc. 130 at 4. While Microsoft may have made this concession merely for the sake of argument, it had the potential to backfire when made elsewhere. For example, in responding to plaintiffs' motion for summary judgment on the ESPP, Microsoft indicated it would not contest the status of plaintiffs as common-law employees. Doc. 152 at 9 n. 6. Magistrate Judge Wilson clearly understood Microsoft's position as such, and recommended a partial verdict for plaintiffs

(Continued on next page)

argument . . . that its earlier concession regarding the common-law employee status of the members of the class was merely arguendo, is without merit. Not only did Microsoft stand by this concession throughout the litigation but the district court also found it was supported by the facts and ruled that Microsoft continued to be bound by it." *Vizcaino III* at 722 (A18).

Microsoft inaccurately asserts that the "named plaintiffs worked for Microsoft between 1987 and 1990; they were classified and treated as independent contractors by Microsoft, and performed a variety of jobs." Pet., p. 6. Microsoft then uses its inaccurate statement regarding the facts of the named plaintiffs to support its argument that "[t]he district court properly excluded from the class the new generation of temporary workers [hired after the so-called "conversion" in April 1990] who had not worked for Microsoft in an independent contractor capacity during the pertinent time period, because the named plaintiffs are not representative of such people." Pet., p. 15.

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in reliance thereon. See Doc. 187 at 30 (indicating that plaintiff employee status was dispositive); id. at 34 (indicating that defendant did not and could not logically contest their employee status). Judge Wilson assumed pre- and post-conversion claims were at issue, id. at 6, 11-12, and defendant did nothing to challenge that assumption.

More important, Microsoft conceded to the Ninth Circuit that plaintiffs were common-law employees, and again did not qualify that concession as applying only to pre-conversion workers. See *Vizcaino II*, 120 F.3d at 1010; *Vizcaino I*, 97 F.3d at 1193 n. 4.

The actual record facts in the district court and court of appeals contradict Microsoft's assertion.

The class representatives in *Vizcaino I, II,* and *III* included Workers employed at Microsoft and both misclassified as "independent contractors" and assigned to third-party "temporary" agencies.[5] It included those at Microsoft *prior* to Microsoft's "conversion" process (*i.e.*, prior to April 1, 1990), and those who worked at Microsoft *after* the 1990 "conversion."[6] The class definition explicitly referred to Workers called employees of "third-party employment agencies." Pet., p. A89 n. 1. Five of the eight *original* class representatives were paid by Microsoft

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[5] In 1994 the magistrate judge said that Microsoft's term "freelancers" means "persons working at Microsoft in either 'independent contractor' or 'temporary agency employee' statuses, who did not receive employee benefits." CR 187, p. 4. This definition was before the court of appeals in *Vizcaino I* and *II*. Similarly, Microsoft told the court of appeals in *Vizcaino I* and *II* (Appellees' Brief, No. 94-35770, p. 1):

> Microsoft has supplemented its regular employees with individuals identified as "freelancers." All of the plaintiffs were classified by Microsoft (and considered themselves) as "freelancers," rather than "regular employees." ER 91-92. *"Freelancers" were persons working at Microsoft in either "independent contractor" or "temporary agency employee" categories, who did not receive employee benefits.* [Emphasis added.]

[6] In April, 1993, Microsoft described the class representatives as "eight individuals who, *during various periods of time between 1987* and the present [*i.e.*, April 1993]," provided "services to Microsoft . . . in positions categorized as freelancers and/or temporary agency personnel." CR 23, p. 2 (emphasis added). There was *no* limitation to those hired before April, 1990.

through third-party agencies *after* April 1, 1990.[7] Furthermore, class representative Jon Waite was originally employed at Microsoft as an "independent contractor" in 1988. CR 9, ¶3. Mr. Waite left Microsoft in 1989, only to be rehired by Microsoft into a different job in August, 1992 and he worked for Microsoft while paid through third-party agencies until he was reclassified as a Microsoft "headcount" employee on April 5, 1993. CR 9 ¶5, 6; CR 90 ¶¶25-27, 31.

All of this information concerning the class representatives' post-1990 employment and employment through third-party agencies was before the district court when the class was certified in 1993, before the court of appeals in *Vizcaino I* and *II*, and before this Court when it denied review in 1998.

Similarly, Microsoft contends (Pet., pp. 11, 26) that the Ninth Circuit should not have decided, "as a matter of law" and "without [a] factual record," that Microsoft, during the course of this case, continued its practice of assigning its own common-law employees to the payroll of "temp" or "payroll service" agencies (a practice known as "payrolling"). See *Vizcaino I* at 1191 (p. A91); *Vizcaino III* at 716 (p. A6). In fact, the *uncontroverted* factual record before the Ninth Circuit in *Vizcaino III* showed that Microsoft had, during this litigation, continued and expanded the same practices that originally resulted in this case and which were discussed in the prior *Vizcaino I* and *II* decisions. Pl. Reply, 9th Cir. No. 98-71388, pp.

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[7] CR 9, ¶¶5-6; CR 11, ¶3; CR 12, ¶3; CR 13, ¶3; CR 14, ¶3.

24-25; CR 345, 349-57. Microsoft simply failed to controvert plaintiffs' evidence on summary judgment.

The 1993 Class Certification

This case was filed as a class action, seeking *inter alia*, prospective injunctive relief. CR 2, ¶16. A class was certified pursuant to FRCP 23(b)(1) and (b)(2), specifically because prospective injunctive relief was sought. CR 47, p. 11. On July 21, 1993, the Court certified a class "for all issues remaining in the case," defined as follows (Pet., p. A89 n. 1):

> All persons employed by the Microsoft Corporation in the United States who are denied employee benefits because they are considered independent contractors or employees of third-party employment agencies, but who meet the definition of employees of Microsoft Corporation under the common law. The definition includes *all* such persons [not limited to those hired after April, 1990] so employed within the applicable statute of limitations. [Emphasis added.]

Expecting to win, and hoping to achieve a broad *res judicata* effect for strategic purposes, Microsoft conceded the correctness of this class definition in the district court and on appeal. *Vizcaino I* at 1190 n. 1 (A89); CR 23, pp. 3, 6. *Microsoft itself acknowledged*, in the class certification briefing in 1993, *prior* to *Vizcaino I* and *II*, *that the class "is not restricted to free lancers or to those with respect to whom determinations [i.e., IRS determinations or Microsoft reclassifications] have been made."* CR 23, p. 4 n. 2

(emphasis added). Accordingly, the entire class of misclassified workers was before the Court in *Vizcaino I* and *II*, not just those who were *personally* "reclassified" or "converted" by Microsoft in 1990.[8]

The magistrate judge who initially considered plaintiffs' claims concluded that Microsoft's incorporation of IRC § 423 into the ESPP meant, as a matter of Washington law, that the ESPP must be extended to all Microsoft common-law employees. *Vizcaino I* at 1191-92, 1197 (A93, A105-A108). The district court disagreed and dismissed the case.

1996-97 Ninth Circuit Decisions Concerning the ESPP

On appeal, *Vizcaino I* explained that the ESPP itself required that it *shall be construed* in accordance with IRC § 423 and this contract construction requirement is part of the contract under Washington law. The ESPP stated (A106):

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[8] The words "IRS-reclassified" and "Microsoft-converted" were neither in the original 1993 class definition, nor even suggested by any party or the district court at the time of class certification. The original class definition also did not require "continuous" employment since 1990 at Microsoft; indeed, the terms of the ESPP itself do not require "continuous" employment. The 1993 class definition also states the class includes *all* persons "so employed within the applicable statute of limitations" (A89 n. 1). Nevertheless, the district court, after remand, imposed *all* of these limitations on class membership. A28, A41-A45. This effectively, as the district court stated, reduced the class to a small "sliver" of the class that previously numbered in the "thousands." A37, A38 n. 3.

> It is the intention of the Company to have the Plan qualify as an "employee stock purchase plan" under Section 423 of the Internal Revenue Code of 1954. *The provisions of the Plan shall, accordingly, be construed so as to extend and limit participation in a manner consistent with the requirements of that Section of the Code.* [Emphasis *by the Court.*]

Vizcaino I held (pp. A106-A113) the ESPP is an offer to all common-law employees of Microsoft who meet the ESPP's eligibility rule incorporating IRC § 423 (*id.* at A106-A107):

> . . . Because the term "employees" in § 423 is construed to refer to "common-law employees," the ESPP, when construed in a manner consistent with the requirements of § 423, extends participation to *all common-law employees* not covered by one of the express exceptions set forth in the plan. Accordingly, *we find that the ESPP, through its incorporation of § 423, expressly extends eligibility for participation to the plaintiff class and affords them the same options to acquire stock in the corporation as all other employees.* [Emphasis added and footnotes omitted.]

The *Vizcaino I* panel also concluded (A109):

> Although Microsoft may have generally intended to exclude individuals who were in fact independent contractors, it could not, consistent with its express intention to extend participation in the ESPP to *all common-law employees,* have excluded the Plaintiffs. Indeed, *such an exclusion would defeat the purpose of including § 423 in the plan, because the exclusion of common law employees not otherwise excepted would*

> *result in the loss of the plan's tax qualification.* [Emphasis added.]

Following the panel decision, the *en banc* Ninth Circuit further stated that Microsoft managers could not exclude the plaintiff class from the ESPP, as a matter of corporate law and contract law (*Vizcaino II* at 1010-11, A63-A65):

> *The ESPP was created and offered to all employees, the Workers knew it, even if they were not aware of its precise terms, and their labor gave them a right to participate in it.* Of course, Microsoft's officers would not allow that participation because they were under the misapprehension that the board and the shareholders had not extended the offer to the Workers. That error on the officers' part does not change the fact that there was an offer, which was accepted by the Workers' labor. Of course, the ESPP provides for a somewhat unusual benefit. An employee, who chooses to participate, must pay for any purchase of stock, and the Workers never did that. We, however, leave the determination of an appropriate remedy to the district court. [Emphasis added; footnote omitted.]

Thus, the Ninth Circuit held in *Vizcaino I* and *II* that Microsoft could not exclude any of its common-law employees from participating in the ESPP without violating the explicit terms of the ESPP and the dictates of Microsoft's shareholders. This was the mandate of the appellate court.

Microsoft sought review by this Court of the merits of these ESPP issues governed by Washington law, as

decided in *Vizcaino I* and *II*, arguing that the Ninth Circuit misapplied Washington law. This Court denied certiorari. 118 S.Ct. 899 (1998).

Proceedings After Remand

Following remand, the district court first decided whether the *Vizcaino* mandate "applies to the entire plaintiff class [both pre-conversion and post-conversion] or only a specific part of it." CR 307, p. 1; 1998 WL 122084, p. 1. In rejecting Microsoft's contention that *only* "pre-conversion" (*i.e.*, pre-1990)[9] claims had been before the Court in *Vizcaino I* and *II*, the district court correctly concluded that "*the mandate* [of the Court of Appeals] *applies to all plaintiffs who were common-law employees, and all periods in which they were common-law employees.*" 1998 WL 122084 at 4 (emphasis added).

Later, in a Microsoft district court reply on its motion to amend class certification (to which plaintiffs were allowed no response), Microsoft included a footnote suggesting the district court should *sua sponte* redefine the class. CR 407, p. 12 n. 10. Without briefing or oral argument, the district court then, *sua sponte*, redefined and drastically reduced the class on July 15, 1998 (almost five

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[9] "Conversion," in Microsoft's terminology, was its process in 1990 of turning misclassified "independent contractors" into either recognized "headcount" employees or assigning them to become "payroll service" or "temporary agency" employees. *Vizcaino I* at 1191 (A91). The named plaintiffs were employed before and after "conversion" and/or were re-hired after "conversion."

years to the day after the original class certification) as follows (A28):

> This case has always been about a particular group of Microsoft workers who share distinct circumstances with the named plaintiffs. The group consists of all Microsoft workers who, like all the named plaintiffs, worked as independent contractors between 1987 and 1990 and whose positions were reclassified as employee positions after the IRS reviewed them. This case, as the Court found in its order on the scope of remand in February, includes the claims brought by the same workers for their work after 1990, when many of them, including four named plaintiffs, were transferred to temporary employment agencies. This is the scope of the plaintiff class.
>
> *Other groups of potential claimants, those who have worked for Microsoft in a non-employee capacity, but were not reclassified by the IRS or converted by Microsoft*, have never, as a practical matter,[10]

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[10] Plaintiffs' facts (rather than facts of unnamed putative class members) were before the district court as a "practical matter" because liability in this class action was, as is normal in a class action, litigated primarily on the named plaintiffs' facts. Therefore, it was incorrect that a substantially reduced class was permitted because "the [revised] definition conforms to the *facts Plaintiffs presented* to the Court." CR 488, p. 4 (emphasis added). Microsoft correctly stated "this is a *class* action" and "[a]bsent class members are not active participants in this action." *Id.*, p. 19 (emphasis by Microsoft). Indeed, Microsoft specifically objected to consideration of factual situations of any Workers other than the named plaintiffs "because the essence of a class action is that it is litigated based upon the facts presented by the representatives of a certified class." CR 376, p. 10.

> *been involved in this case. At this time, they remain outside the plaintiff class.* [Emphasis added.]

The district court's class redefinition thus imposed major new limitations upon class membership that were never in the original 1993 stipulated class definition, *i.e.*, it added requirements that each class member be hired before April 1, 1990, and also be either "reclassified" by the IRS or "converted" by Microsoft. The district court thereby excluded the vast majority of original class members from participating in the fruits of the victory won by the class in *Vizcaino I* and *II*. The excluded workers were thus forced to pursue many *individual* claims, potentially *thousands*, by mass interventions in this action or by separate lawsuits. CR 553; Pet., p. 10 n. 6. Creation of such obstacles to relief effectively rewarded Microsoft for continuing and expanding its breach of the ESPP contract after this lawsuit began.

REASONS FOR DENYING THE WRIT

I.

THE NINTH CIRCUIT'S DISCRETIONARY USE OF MANDAMUS IN WHAT MICROSOFT AGREES IS ITS "TRADITIONAL" FUNCTION – "TO ENFORCE THE LAW OF THE CASE" – CANNOT BE A DEPARTURE FROM "THE ACCEPTED AND USUAL COURSE OF JUDICIAL PROCEEDINGS" AND, CONSEQUENTLY, DOES NOT COMPEL THE "EXERCISE OF THIS COURT'S SUPERVISORY POWER" TO REVIEW WHETHER THE NINTH CIRCUIT MISUNDERSTOOD ITS OWN PRIOR MANDATE UNDER WASHINGTON LAW.

Microsoft agrees that a "traditional office of mandamus is to enforce the law of the case doctrine" and make sure a lower court carries out a decree by a higher court in the same case. Pet., p. 21, citing *In re Blake*, 175 U.S. 114, 117 (1899), and *Sibbold v. United States*, 37 U.S. 488, 492 (1838). This is precisely what occurred here. Pet., p. 3; *Vizcaino III* at 719-20 (A11-A12).

Microsoft also agrees that issuance of a writ is a matter within the appellate court's discretion. *Id.* at 719-20 (A12), citing *Kerr v. U.S. District Court*, 426 U.S. 394, 403 (1976). Microsoft thus must show that the Ninth Circuit so thoroughly misunderstood its own mandate that it abused its discretion and it went "so far" beyond the "accepted and usual course of judicial proceedings" as to compel both this Court's review and this Court's independent construction of the Ninth Circuit's prior mandate (Pet., p. 22 and n. 10), even though review of the *substance* of that prior Ninth Circuit mandate was previously denied by this Court, 118 S.Ct. 899 (1998).

Here, the Ninth Circuit in *Vizcaino III* carefully reviewed the scope of its prior mandate (A14):

> The class certification is a central premise of both [prior] opinions. Thus, in *Vizcaino I*, the panel relied on the Magistrate Judge's finding that "Microsoft conceded the fact that the named plaintiffs and the class they represent generally were common law employees" and that Microsoft "reserved only the right to object to the employment status of particular plaintiffs during certain periods of their tenure with Microsoft." 97 F.3d at 1193 n. 4. It went on to "hold that the named plaintiffs and the class they represent are covered by the specific provisions of the ESPP." *Id.* at 1197. In *Vizcaino II*, the en banc court states that "the ESPP must, essentially, be made available to all employees" and "[t]he ESPP was created and offered to all employees." 120 F.3d at 1011, 1014. And the class is an integral element of the mandate which remanded "for the determination of any questions of individual eligibility for benefits that may remain following issuance of this opinion and for calculation of the damages or benefits due the various class members." *Vizcaino I*, 97 F.3d at 1200; see also *Vizcaino II*, 120 F.3d at 1015 ("Any remaining issues regarding the rights of a particular workers in the ESPP and his available remedies must be decided by the district court upon remand."). Thus, the district court's statement that this case is about a particular group of Microsoft employees who share "distinct circumstances" is unfounded.

Thus, the Ninth Circuit held in *Vizcaino III* that in *Vizcaino I* and *II* the district court was instructed that "all employees" of Microsoft (as "employee" is defined in the

common law) are entitled to participate in the ESPP, by the terms of the ESPP itself, as construed under Washington State law. *Vizcaino III* at 720-21 (A14). The court of appeals further held *in Vizcaino III* that *"the class* [as originally defined] *is an integral element of the mandate"* in *Vizcaino I* and *II* (A14, emphasis added).

Microsoft only slightly quibbles with the correctness of the Ninth Circuit's explanation of its own prior decisions and mandate. It contends the Ninth Circuit did not expressly limit the district court's authority to substantially decertify the class in its remand for the district court's "determination of any questions of individual eligibility for benefits" and its calculation of amounts due these individuals. Pet., pp. 21-22. It does not dispute, however, that the mandate includes both matters explicitly *and* implicitly decided. *E.g., Firth v. U.S.*, 554 F.2d 990, 994 nn. 3-4 (9th Cir. 1977); *In re Chambers Development Corp.*, 148 F.3d 214, 224 (3d Cir. 1998).

Microsoft maintains the mandate of *Vizcaino I* and *II* is not "obvious" and therefore it scolds the Ninth Circuit for deciding the question of the district court's compliance with those prior decisions and mandate by way of mandamus instead of by an eventual appeal. Pet., p. 22. Of course, such an appeal would occur only long after the harm addressed in *Vizcaino III* had already occurred – *i.e.*, former class members who had prevailed on appeal in *Vizcaino I* and *II* were being forced to pursue thousands of individual claims to win the same relief they had previously won on appeal as class members.

There was no abuse of discretion by the Ninth Circuit in utilizing the mandamus procedure to enforce its own

prior mandate since, Microsoft agrees, this is a traditional and proper function of mandamus.[11] Pet., p. 21. Furthermore, the Ninth Circuit did not misunderstand its own

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[11] Whether the court of appeals should have exercised its mandamus power does not present a compelling issue for this Court's review for two additional reasons. First, the mandamus petition in *Vizcaino III* was consolidated with an appeal of the district court's denial of a permanent injunction (Pet., pp. A9-A10). The court of appeals undisputedly had jurisdiction over the permanent injunction appeal. 28 U.S.C. § 1292(a)(1). An injunction appeal brings up for review any underlying matters "inextricably intertwined" with the injunction order from which the appeal is taken. *Thornburgh v. Amer. College of Obs. and Gyn.*, 476 U.S. 747, 755-57 (1986) (court of appeals reviewing district court's ruling on preliminary injunction properly reviewed merits as well); *Deckert v. Independence Shares Corp.*, 311 U.S. 282, 287 (1940) (court of appeals reviewing order granting preliminary injunction also had jurisdiction to review order denying motions to dismiss). The district court denied plaintiffs' application for a permanent injunction primarily because class members excluded by the district court's class redefinition order had not yet "prevailed." Pet., pp. A9-A10. Thus, the correctness of the class redefinition was before the court of appeals in the injunction appeal and that court would have been required to address these same issues in that appeal regardless of whether it exercised its mandamus powers. *Vizcaino III* explained (A24): "[b]ecause our opinion also disposes of the issues raised in plaintiffs' appeal from the denial of a permanent injunction, we DISMISS that appeal without prejudice." Accordingly, even if the court of appeals had abused its discretion in exercising its mandamus powers, plaintiffs' permanent injunction appeal involving the same issues would still need to be decided by that court.

Second, this sort of procedural issue may no longer arise since FRCP 23(f) was amended effective Dec. 1, 1998 to allow interlocutory review of certain class certification rulings. This amended rule was not in effect until after the district court's 1998 rulings were entered and the mandamus petition filed.

prior mandate and there was no departure from the accepted course of judicial proceedings that compels review by this Court. Indeed, the Ninth Circuit was entirely correct in enforcing its own prior mandate and *not even the dissenters* on the merits from the prior mandate in *Vizcaino I* and *II* voted to rehear the *Vizcaino III* enforcement order. 184 F.3d 1070.

II.

THE NINTH CIRCUIT APPLIED ESTABLISHED PRINCIPLES UNDER RULE 23(c)(1) IN HOLDING THAT THE DISTRICT COURT SHOULD NOT HAVE SUBSTANTIALLY DECERTIFIED A CLASS AFTER THE CLASS PREVAILED IN TWO NINTH CIRCUIT DECISIONS ON THE MERITS UNDER WASHINGTON STATE LAW.

Microsoft contends the Ninth Circuit made "a significant misapplication of Rule 23" and it thus abused its discretion in preventing Microsoft from repudiating its previous explicit waiver of any dispute over the class definition.[12] Pet., pp. 13-20. Because the Court does not review alleged "misapplication[s]" of established principles of civil procedure, S.Ct. Rule 10, Microsoft must demonstrate with "compelling reasons" that the alleged "misapplication" of Rule 23 in the decision below was such an extraordinary departure "from the accepted and usual course of judicial proceedings . . . as to call for an

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[12] Microsoft argues "it was error here to forbid the district court" from changing the class on remand even though, "at the very outset of this action, the parties may have agreed" on the class definition. Pet., p. 15.

exercise of this Court's supervisory power." S.Ct. Rule 10(a). Microsoft makes no such showing of "compelling reasons" for review; indeed, the decision below was completely consistent with all relevant authorities.

First, Microsoft argues that all class certification orders are inherently "provisional" and may be changed "at any time before final judgment," even *after* a decision "on the merits," as there was here. Pet., pp. 16-17. The Ninth Circuit rejected Microsoft's position, following the precise language of Rule 23, which provides a class certification "may be altered or amended *before the decision on the merits.*" Rule 23(c)(1) (emphasis added). The Ninth Circuit, following other circuits, held that a class-wide appellate decision "on the merits" of liability issues, leaving only "questions of individual eligibility" and calculations of amounts due, is a "decision on the merits" within Rule 23(c)(1) even though such individual calculations may remain at issue until final judgment under Rule 23(c)(3).[13] *Vizcaino III* at 721 (A15-A16) explained:

> Rule 23(c)(1) permits a certification order to be altered or amended "before the decision on the merits," not afterward. See *Scott v. City of Anniston*, 682 F.2d 1353, 1357 (11th Cir. 1982)

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[13] Microsoft cites (Pet., p. 17) authorities indicating that a class may be decertified in a few situations, *e.g.*, 5 *Newberg on Class Actions* § 24.71, pp. 24-228 to 229 (3d ed. 1992), where the plaintiffs turned out to have a conflict of interest or otherwise were inadequate representatives. In such cases, the class should not be bound by *res judicata*. Here, the representative plaintiffs were not only "adequate," they were successful. There could be no basis for the district court to deny *Vizcaino I* and *II* class members the fruits of their class-wide victory in the Ninth Circuit based on "adequacy" of the representation.

> (ruling that appellate decision finding evidence sufficient to make prima facie case and insufficient to sustain proferred defense and remanding for further proceedings as to individual class members' damages was a "decision on the merits" precluding subsequent class modification under Rule 23(c)(1); *Jimenez v. Weinberger*, 523 F.2d 689, 697 (7th Cir. 1975) (holding that Rule 23(c)(1)'s "explicit permission to alter or amend a certification order before decision on the merits plainly implies disapproval of such alteration or amendment thereafter"). This court's prior decision adjudicates the merits of the plaintiff class' claim, leaving only "questions of individual eligibility for benefits that may remain . . . and calculation of the damages or benefits due the various class members." *Vizcaino I*, 97 F.3d at 1200.

Second, Microsoft quarrels with the Ninth Circuit's account of the proceedings, contending (Pet., p. 14) the Ninth Circuit was wrong in finding (*Vizcaino III* at 721, A16) that Microsoft had conceded the commonality and typicality issues it argues now and it was wrong (Pet., pp. 17-18), in finding (*Vizcaino* III at 722, A18) that Microsoft agreed the Workers are generally common-law employees of Microsoft, with potential individual exceptions. These findings are more than amply supported by the record, as explained by the court of appeals.

Moreover, the Ninth Circuit pointed out Microsoft's hypocrisy on this matter. Microsoft maintains the 1994 decisions of the district court *in favor of Microsoft* which were not appealed (and thus were not reversed) may not be relitigated by the original class. CR 363 at p. 5. *Vizcaino III* explained that Microsoft cannot have it both ways,

claiming the benefits of a class-wide decision *for Microsoft* while denying any effect to the class-wide decision of the Ninth Circuit *against Microsoft* (at 720, A13):

> [If Microsoft had won on all the issues and] the judgment had not been reversed, it would have been preclusive as to all the workers now excluded from the class under the district court's revised class certification. Were the case before us now in that posture – i.e., had this court affirmed rather than reversed – there is little doubt what Microsoft's position would be as to who is included in the class. Microsoft's argument that the scope of the class was not material to the issue on appeal is not tenable for that reason alone – substantial rights were at issue for all the members of the certified class.

Third, Microsoft contends that the district court was correct in substantially decertifying and drastically reducing the class because this made sure the class was represented "appropriately" and "adequately." Pet., p. 19. There are, however, only various *immaterial* differences between the remaining "sliver" of the class and the much larger excluded part of the former class, basically (1) the particular years they worked and (2) whether *Microsoft*, in retrospect, *admitted* they were in the class.[14] These

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[14] The latter point – "Microsoft's admissions" – was emphasized by the district court (p. A44). Accordingly, the district court effectively limited the plaintiff class to only those Microsoft still *agreed on*, thereby excluding from the class many who had prevailed on appeal *against Microsoft* because Microsoft did not agree, pp. A44-A45. To limit the class, after

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"distinct circumstances" (Pet., p. 19 and A28) had no relationship whatsoever to the class claims or their entitlement to benefits. Class certification under Rule 23 is based upon common claims and common questions of law and fact, not on *identical* facts. FRCP 23(a); see, *e.g., In Re Prudential Ins. Co. of Am. Sales Prac. Lit.*, 148 F.3d 283, 311 (3d Cir. 1998); *Forbush v. J.C. Penney Co.*, 994 F.2d 1101, 1105 (5th Cir. 1993). The existence of non-material factual differences does not preclude class certification in the first instance, and it is even less reason for substantial decertification of an existing class that already prevailed on the merits. Rule 23(c)(1). Moreover, the district court did not give notice to the class of the possibility of decertification before the class definition was changed and it refused to give the larger excluded part of the class an opportunity to add "appropriate" additional class representatives. CR 553.

Finally, Microsoft raises a point that it never presented to the district court or the Ninth Circuit and therefore could not be appropriate for review by certiorari, *i.e.*, that class members should have "been given individual notice of the action [and] the opportunity to opt out of the class." Pet., p. 19, *citing Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 812 (1985), and *Ortiz v. Fibreboard Corp.*, 119 S.Ct. 2295, 2313 (1999). This is, however, as Microsoft expressly *agreed* in 1993, a class action under Rule 23(b)(1)(A) and (b)(2) and these categories are

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success on the merits, to only those the defendants "admits" should prevail is not consistent with the district court's responsibility to protect the class. *Deposit Guar. National Bank v. Roper*, 445 U.S. 326, 331 (1980).

undisputedly appropriate in light of plaintiffs' pending request for injunctive relief (A9-A10, A18-A19, A24). This was *not* a Rule 23(b)(3) "opt-out" class action. Moreover, Microsoft itself successfully *opposed* giving any notice about this case to the class in the district court. CR 57.

Ortiz was certainly correct in holding that a Rule 23(b)(3) "opt-out" class action could not be converted into a Rule 23(b)(1)(B) mandatory class action through a settlement by the parties which arbitrarily established a "limited fund" by simply agreeing to a "limited" settlement amount. This class here, however, is not a settlement class, nor is this a "limited fund" case. Due to the need for declaratory and injunctive relief, this is properly a class action under Rule 23(b)(1)(A) and (b)(2). Microsoft does not argue otherwise.

Moreover, the district court here did *not* give thousands of class members a chance to *"opt out."* Rather, *it simply expelled them* from the class without giving them notice, and without providing any chance to propose new class representatives as Microsoft itself had suggested (CR 407 at p. 8).[15] Moreover, the district court ruled that thousands of workers who had been in the original class that prevailed in the Ninth Circuit must *individually* intervene or file new lawsuits to pursue the *same* claims on which they had, as class members, already prevailed in the Ninth Circuit. A9; CR 553.

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[15] The district court denied plaintiffs' request to name additional class representatives who were working in the period from 1989-98 in positions covered by the original class definition. *Vizcaino III* at 718 (A9).

Thus, the Ninth Circuit's *Vizcaino III* decision is not such a "far" departure from "the accepted and usual course of judicial proceedings" as to compel the "exercise of this Court's supervisory power," S.Ct. Rule 10(a), nor is it in conflict with any other circuits on the application of Rule 23(c)(1) to appellate decisions on the merits in favor of class. It is also completely consistent with numerous decisions holding similar claims are certified as class claims under Rule 23(b)(1)(A) and (b)(2). Finally, the Ninth Circuit was entirely correct, on the record in this case, in finding that Microsoft repeatedly waived any dispute concerning the class certification.

III.

THE NINTH CIRCUIT'S THREE DECISIONS IN *VIZCAINO I, II* AND *III* ARE ALL BASED ON WASHINGTON STATE COMMON LAW PRINCIPLES, THIS COURT ALREADY DENIED CERTIORARI ON THE MERITS OF THOSE STATE LAW ISSUES IN 1998, AND MICROSOFT'S EFFORTS TO PROMOTE SOME SORT OF FEDERAL COMMON LAW TO OVERRIDE WASHINGTON'S COMMON LAW OF CONTRACTS SHOULD BE REJECTED PURSUANT TO *ERIE RAILROAD V. TOMPKINS*.

This Court does not review the application of issues of state law which a petitioner may contend were wrongly decided by the court of appeals. S.Ct. Rule 10. The parties here agreed that the ESPP issues in *Vizcaino I* and *II* were governed by Washington State law. *Vizcaino I* at 1196 (A105); *Vizcaino II* at 1014 (A64). This Court denied certiorari in 1998 when Microsoft previously sought review of these *same* Washington law issues

concerning the ESPP. No. 97-854, 118 S.Ct. 899 (1998).[16] Now, after the Ninth Circuit enforced and reiterated some aspects of those same decisions under Washington law in *Vizcaino III*, Microsoft disregards Washington law and urges the Court to create a *federal common law* of employee benefits to override state law.[17]

Microsoft argues there should be some sort of federal common law of employee benefits contracts that "restor[es] order to the law of employee benefits" (evidently for the computer industry in particular). Pet., pp. 4 and n. 2, 24-27. Microsoft contends there needs to be a common federalized "order" for all employee benefit cases, including this contract case under Washington common law, to provide, among other things, for "orderly resolution" of two cited pending district court ERISA cases. Pet., pp. 4 n. 2 and 24-27.[18] Microsoft's position is contrary to *Erie*

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[16] The Petition for Certiorari and the Respondents' Brief in Opposition in No. 97-854 discuss the Washington State law issues presented in *Vizcaino I* and *II*.

[17] Microsoft argues that *Vizcaino III* dealt with the merits of ERISA claims governed by federal law, as well as ESPP claims governed by Washington state law. Pet. p. 12. This is incorrect because *Vizcaino II* remanded ERISA claims to the plan administrator (A63, A66), and those claims were further remanded by the district court on Feb. 13, 1998 (1998 WL 122084, p. 4). The plan administrator did not complete review until Sept. 28, 1999.

[18] Microsoft cites two pending district court cases in New York and Los Angeles as the reason why this Court should review the merits of the Washington common law issues in *Vizcaino III*. Pet. 4 n. 2. Both cited cases are ERISA cases at a very early stage, *e.g.*, *Herman v. Time-Warner*, 56 F.Supp.2d 411

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Railroad v. Tompkins, 304 U.S. 64 (1938), which held there can be no federal common law governing such claims arising under state law and the federal courts will apply state law to state law claims such as those here.

Microsoft further contends that the Ninth Circuit was wrong in relying on IRS employee status determinations for several positions to create a presumption of employee status for workers in those IRS-reclassified positions, thereby shifting the burden of proof to Microsoft to establish any exceptions. Pet., pp. 11, 20, 25. This is, first of all, exactly what Microsoft agreed to. The IRS determinations covered job classifications, not individuals.[19] Microsoft

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(S.D.N.Y. 1999). Microsoft does not explain how this Court's decision on the Washington common law of contracts could affect those ERISA cases, nor does it even try to show how its proposal for a federal common law of non-ERISA state law contractual employee benefits would cause an "orderly resolution" of cases under ERISA. It certainly does not propose any compelling reason to overrule *Erie Railroad v. Tompkins*.

[19] The 1989 Internal Revenue Service examinations of certain types of Microsoft workers determined common-law employee status based upon job *positions*, stating for example:

> As a result of our Federal Employment Tax examination, we have determined that services performed for Microsoft *by an individual in the position commonly referred to as* "Formatter" constitute an employer-employee relationship. This determination is *based on information received from Microsoft and on information received from a representative sampling of the workers in that job position* . . .
>
> *This determination covers the employment position* named in the first paragraph of this letter *and all*

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expressly accepted these findings, agreeing to "review other *job positions* to insure compliance." CR 444, p. 004195. Moreover, Microsoft agreed in this case that these workers were "generally" employees of Microsoft. *Vizcaino I* at 1193 n. 4 (A96); *Vizcaino II* at 1010 (A53); *Vizcaino III* at 722 (A18). The burden was thus correctly placed on Microsoft in *Vizcaino I* at 1193 n. 4, 1200 (A96, A113-A114), which this Court declined to review. 118 S.Ct. 899 (1998). In light of Microsoft's general concessions, placing the burden on Microsoft to prove specific exceptions is both logical and consistent with the rule that a class action defendant that has been found responsible for a pattern and practice of conduct must prove any specific exceptions. *Cf. Internat'l Brotherhood of Teamsters v. United States*, 431 U.S. 324, 359 (1977). Nevertheless, following remand, the Workers also submitted extensive uncontroverted evidence in support of summary judgment as to the common-law employee status of the IRS-reclassified job positions at Microsoft. Microsoft neither controverted nor rebutted that evidence. Thus, consistent with Rule 56 and *Celotex Corp. v. Catrett*, 477 U.S. 317, 322 (1986), the Ninth Circuit was correct in its determinations that the workers in Microsoft's IRS-reclassified positions are entitled to participate in the ESPP.

> *differently named positions that are substantially similar in nature*. This determination pertains to all tax periods beginning after December 31, 1985. (Emphasis added.)

"Formatter" is but one of the *positions* reviewed by the IRS, and is used here for purposes of explaining the IRS approach to determining common-law employee status by *position*. CR 444, p. 004298. The panel decision in *Vizcaino I* at 1190 n. 2 (A91) quoted this language from the IRS letters.

Microsoft's argument that the Workers are seeking double benefits (from Microsoft and its payroll agencies) is groundless; plaintiffs are seeking Microsoft employee benefits to which they are entitled, under governing Washington State law, by the explicit terms of Microsoft's plan. *Vizcaino II* at 1014 (A63-A65); *Vizcaino I* at 1196-97 (A105-A108). Microsoft "payrolled" the workers through agencies to *deny* them employee benefits, *not* to give them "benefits" through its payroll agencies. *Vizcaino I* at 1191 (A91-A92). There is *no* record evidence that an employee of Microsoft (as the Workers are) could obtain duplicate ESPP benefits through the payroll agencies, nor is there any record evidence that the payroll agencies offer any such benefit. All that the Ninth Circuit said (A19), as a subsidiary alternative point, was that, *hypothetically*, "[e]ven if" Microsoft could somehow push the Workers into some kind of employment relationship with the agencies by payrolling the Workers through these "paymaster" agents, as they are defined in Washington law, see *Rho Co. v. Dep't of Revenue*, 782 P.2d 986, 992-93 (Wash. 1989), this would not destroy the Workers' common-law employee status at Microsoft. *Vizcaino III* at 723 (A19-A20).

For this subsidiary alternative point, the Ninth Circuit cited Washington law and tax law cases, including tax law principles which were expressly incorporated into the ESPP by Microsoft. *Vizcaino I* at 1196-97; *Dopps v. Alderman*, 121 P.2d 388, 391 (Wash. 1942) (federal statute affecting "construction" of contract is incorporated into and "becomes a part" of the contract, under Washington contract law); *Boggs v. Whitaker*, 784 P.2d 1273, 1274-75 (Wash.App. 1990). This point is also consistent with general common law principles. *NLRB v. Town & County Elec.*, 519 U.S. 85, 94-95 (1995).

Finally, Microsoft's allies in the *amici* brief of ITAA *et al.* propose some sort of federal common law to override Washington law, based on the tax law concept of "leased employees." Aside from running directly against this Court's instructions in *Erie Railroad, supra,* that there is no federal common law for state law claims, there are no "leased employees" in this case. Common-law employees of Microsoft, members of the class here, cannot by definition also be "leased employees" of Microsoft at the same time. *Burrey v. Pacific Gas & Elec.*, 159 F.3d 388, 393 (9th Cir. 1988); 26 USC § 414(n)(2).

CONCLUSION

The petition does not establish any compelling reasons to review the court of appeals' enforcement of its own mandate based on Washington State law, particularly where review of that mandate itself was previously denied. 118 S.Ct. 899 (1998). The petition should be denied.

DATED: November 19, 1999.

Respectfully submitted,

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IN THE

Supreme Court of the United States

MICROSOFT CORPORATION, *et al.*

Petitioner,

v.

DONNA VIZCAINO, *et al.*

Respondents.

ON PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

PETITIONER'S REPLY BRIEF

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LIST OF PARTIES AND RULE 29.6 STATEMENT

There have been no changes in the information previously submitted by Microsoft Corporation, pursuant to Rule 29.6, in its petition for certiorari.

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Rather than address the significant issues of class management and employment law raised by Microsoft's petition, Respondents change the subject, primarily by insisting that Microsoft "conceded" the scope of the class and the common law employee status of all its purported members. Respondents' pleas in avoidance grossly misstate the proceedings below.

First, Microsoft's concession (which the en banc *Vizcaino II* court agreed was arguendo, 120 F.3d at 1010 (A53)) pertained at most to the named plaintiffs and those they represented at the time this case was certified in 1993, i.e., former freelancers. It did not pertain to the thousands of temporary workers who performed services at Microsoft under different conditions during the intervening six years and who, as the District Court so correctly held, were never intended to be part of the class. Even had the concession not been limited, the recent

decision in *Ortiz* v. *Fibreboard Corp.*, 119 S. Ct. 2295 (1999), confirms that no party's agreement can circumvent Rule 23's command that class members share the named plaintiffs' essential traits. *Id.* at 2315 n.24 (noting "the constitutional requirement" that district courts ensure that "'named plaintiffs at all times adequately represent the interests of absent class members'") (quoting *Phillips Petroleum Co.* v. *Shutts*, 472 U.S. 797, 812 (1985)).

Second, because the *Vizcaino II* court ignored the class scope, the issuance of mandamus in *Vizcaino III* creates a rule forbidding District Courts from enforcing Rule 23 after a remand in all cases.

Third, contrary to Respondents' muddled arguments misrepresenting both the record and *Erie Railroad* v. *Tompkins*, 304 U.S. 64 (1938), the decision in *Vizcaino III* allowing dual benefit packages for temporary workers is based on a misinterpretation of the Internal Revenue Code and ERISA and thus presents a question of federal law. Moreover, certiorari is particularly apt because the Ninth Circuit's conclusion, that temporary agency employees presumptively have a common law employment relationship with both their agency and the agency's client permitting them to receive benefits from both, conflicts with the Tenth Circuit's decision in *Roth* v. *American Hospital Supply Corp.*, 965 F.2d 862, 867 (10th Cir. 1992) (holding that an employee has only one employer for purposes of ERISA benefit entitlement).

I.

Vizcaino III Interferes with District Courts' Constitutional Duty to Ensure that Rule 23 Is Satisfied at All Times Before Final Judgment

Because they cannot, Respondents do not directly contest this Court's holdings that a District Court has the

obligation to "adjust the class, informed by the proceedings as they unfold," in order to assure that a class complies with Rule 23's prerequisites. *Amchem Prods., Inc.* v. *Windsor*, 521 U.S. 591, 620 (1997). Instead, they resort to semantics and misrepresent the record to convey the false impression that the class certified in 1993 was drastically "reduced" in 1998.

In fact, the opposite is true. Because four years had passed between its class order and remand from the Ninth Circuit — a time of unprecedented expansion in Microsoft's industry — the District Court was faced with a situation in which a class definition meant to encompass a few hundred individuals could now plausibly be read as including many thousands of others not contemplated at the time of certification. The District Court could not have been clearer in ruling that the class was not being "reduced" but instead that it continued to be composed only of those workers who, like the named plaintiffs, had been the subjects of the IRS's rulings.[1] The District Court thus made certain that Rule 23's requirements of commonality and typicality were satisfied, by ensuring that class members "at all times" shared the essential

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[1] *E.g.*, A28 ("This case has always been about a particular group of Microsoft workers . . . who, like all the named plaintiffs, worked as independent contractors between 1987 and 1990"); A38 n.3 ("Clearly, the Court understood the proposed class to consist only of the freelance workers that the IRS determined were Microsoft employees in 1989"). This understanding of the scope of this class is, moreover, explicit in the certification order: the District Court found that the class presented "common issues" because "[t]he Internal Revenue Service has already made a determination that [the class members] are common law employees for tax purposes." (7/21/93 Order at 11.)

characteristics that had qualified the named plaintiffs as class representatives. *Ortiz*, 119 S. Ct. at 2315 n.24.[2]

Unable to contest the substance of these issues, Respondents instead insist that the District Court was barred from enforcing Rule 23 on the theory that the *Vizcaino II* remand constituted "the decision on the merits" within the meaning of Rule 23(c)(1). In doing so, they ignore this Court's holding that the phrase "the decision on the merits" used in Rule 23 means "final judgment." *See Gardner* v. *Westinghouse Broad. Co.*, 437 U.S. 478, 480 n.6 (1978) ("a decision on class-action status may be conditional, subject to alteration or amendment prior to final judgment, F. R. Civ. P. 23(c)(1)") (internal quotation marks omitted). The Ninth Circuit and Respondents are simply wrong in concluding that *Vizcaino II* constituted the decision on the merits within the meaning of Rule 23: in addition to remanding the entire SPP claim without making even a partial determination as to liability, *Vizcaino II* ordered, inter alia, extensive proceedings to determine each putative class members' common law employment status. *E.g.*, *St. Louis, Iron Mountain & S. R.R.* v. *Southern Express Co.*, 108 U.S. 24, 28-29 (1883) (a final judgment "terminates the litigation between the parties on the merits of the case, and leaves nothing to be done but to enforce by execution what has been determined").

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[2] Respondents' suggestion that there are "only various *immaterial* differences" between the former freelancers and the temporary agency workers (Opp'n at 21) ignores the substantial dissimilarities between the two groups outlined in Microsoft's petition. (*See* Pet. at 25 (noting distinctions regarding the method of payment, provision of employee benefits, tax treatment, training, and recruitment).) Microsoft submitted extensive documentation detailing these disparities, contrary to Respondents' false contentions of uncontroverted evidence.

Even more egregious is Respondents' error in contending that the District Court was barred from enforcing Rule 23 because Microsoft purportedly "conceded" that the class encompassed every temporary agency employee who had been or would be assigned to work at Microsoft. (Opp'n at 20.) Not only did Microsoft make no such concession,[3] Rule 23 charges District Courts with the responsibility to protect the interests of absent class members without regard for what the parties agree to. *Ortiz*, 119 S.Ct. at 2316 ("uncritical adoption" of facts "agreed upon by the parties" to demonstrate propriety of class certification "is no substitute for rigorous adherence to those provisions of the Rule 'designed to protect absentees'") (quoting *Amchem*, 521 U.S. at 620). Respondents' repetition of the Ninth Circuit's gratuitous supposition that "there is little doubt" that Microsoft would have urged an expansive class scope had it prevailed, *Vizcaino II* at 720 (A13), is not only baseless, it illustrates the wisdom of Rule 23 and *Ortiz*'s rule, which requires the District Court, not one or more self-interested parties, to determine the scope of the class.[4] Thus, even if Microsoft and Respondents had agreed upon a class, that agreement would not affect the District Court's independent duty to

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[3] Respondents misleadingly quote a fragment of a footnote in a prior brief by Microsoft to suggest that Microsoft conceded the class scope. As the sentence in which the footnote reference appears shows, however, Microsoft expressly objected to class treatment of issues such as employment status. (4/19/93 Resp. at 4 ("[if plaintiffs are not precluded from receiving benefits by the fact that they were never offered benefits and actually promised they would not seek benefits,] a separate determination would be required as to (1) Whether each prospective class member was, in fact, a common law employee of Microsoft").)

[4] Furthermore, the hypothesis proves too much, for by parity of reasoning Respondents would have taken the position that the class was as narrow as possible, had they lost.

ensure that Rule 23 is met, right up to the entry of final judgment.

Respondents also fail to confront the negative ramifications of *Vizcaino III*'s expansion of a mandatory class that is without the notice and opt-out protections that safeguard non-mandatory classes. Unable to dispute that the Due Process Clause forbids mandatory class treatment of actions that are "predominately for money damages," *Phillips Petroleum Co.* v. *Shutts*, 472 U.S. 797, 812 n.3 (1985), Respondents argue that *Shutts*'s constitutional protections are inapplicable because of their "pending request for injunctive relief." (Opp'n at 23.) While their 1992 Complaint did request injunctive relief in addition to money damages, in the intervening seven years this case plainly has become one "predominately for money damages," as shown by *Vizcaino II*'s identification of monetary issues for decision on remand. An incidental request for injunctive relief does not save the mandatory class from being constitutionally repugnant.[5]

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[5] Respondents are wrong in claiming that this Court may not address the inappropriateness of mandatory class treatment of this action because Microsoft did not raise this objection below. This class was first created by the Ninth Circuit in *Vizcaino III*, so Microsoft had no opportunity to object previously to its contours. Moreover, Respondents' error is compounded by the Ninth Circuit's rule that such a determination can be reviewed collaterally. *See Brown* v. *Ticor Title Ins. Co.*, 982 F.2d 386, 392 (9th Cir. 1992), *cert. granted*, 510 U.S. 810 (1993), *cert. dismissed*, 511 U.S. 117 (1994) (as a matter of due process, an absent member of an improperly certified mandatory class is *not* barred by res judicata from relitigating a claim involving "substantial money damages").

II.

The Ninth Circuit's Holding Makes the Class Definition Part of Every Mandate, and Thus Has Significant Ramifications on All Class Action Litigation

Although Respondents cite several black-letter rules regarding mandate standards, they cannot establish that the prior appeal constituted a ruling on the class definition because, as Microsoft explained in its petition, no fair reading of the mandate draws the propriety of the class into question. Neither *Vizcaino I* nor *Vizcaino II* makes any mention of the class definition other than to recite it verbatim, none of the opinions mentions Rule 23, and the holding of the Circuit Court would have been the same regardless of the scope of the class.

Respondents' attempts to downplay the importance of the Ninth Circuit's abuse of its mandamus powers grossly understate the consequences of the Ninth Circuit's overreaching. If *Vizcaino II* — which makes the barest mention of the class scope — is read to preclude ongoing enforcement of Rule 23, every appellate court remand in a class action will fix in stone the original class certification. Neither the changes in Rule 23(f) nor the eventual availability of appeal softens the blow to enforcement of Rule 23. Consequently, prudent litigants will be compelled to appeal and cross-appeal the issue of class certification at every turn in order to avoid a class definition that may prove unworkable in light of subsequent factual developments. Restated in *Vizcaino III* parlance, all litigants will be forced to file a "contingent cross-appeal" of any class certification, thereby needlessly proliferating appeal issues.[6]

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[6] Respondents do not even attempt to defend the Ninth Circuit's conclusion that Microsoft is barred from contesting the

III.

The Ninth Circuit's Finding that a Temporary Agency Employee Is Presumptively a Common Law Employee of both the Agency and the Agency's Client Is Wrong as a Matter of Federal Law

Even Respondents do not offer support for the Ninth Circuit's conclusion that a temporary agency employee's relationship with the agency is irrelevant to the issue of whether he or she is a Microsoft employee and, consequently, a temporary agency employee is presumptively a common law employee of both the temporary agency and the agency's client. Nor do Respondents endorse *Vizcaino III*'s contravention of the Internal Revenue Code, which provides that temporary agency employees are employees of either the temporary agency *or* the temporary agency's client, I.R.C. § 414(n)(2) — notwithstanding that a purported desire to enforce the Code is the basis of *Vizcaino I* and *II*. (*See* A63, A106) This is hardly surprising because the District Court, Respondents, and Microsoft all agreed that the relevant inquiry was whether the temporary agency *or* Microsoft was the employer. The Ninth Circuit's holding on this issue was entirely sua sponte and sui generis.[7]

Unable to defend on substantive grounds, Respondents seek to shield the Ninth Circuit's holding from review by — once again — retreating to the claim

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propriety of the class certification as a result of Microsoft's failure to take a "contingent cross-appeal" of the certification order.

[7] *See also* Alvin D. Lurie, *Microsoft Re-re-redux: New Twist of the Eternal Triangle*, 84 Tax Notes 143, 147 (1999) (presumptively "the existence of a bona fide employment relationship with Company B would preempt an employment arrangement with Company A as to the identical services").

that, in 1994, Microsoft conceded that it was the common law employer of every temporary agency employee who had worked or ever would work at Microsoft. (Opp'n at 27.) The Ninth Circuit, however, did not find that Microsoft had conceded the issue;[8] it concluded as a matter of substantive law that the temporary agency workers were presumptively Microsoft's employees.

Respondents further claim that the Ninth Circuit's novel principle of employment law is based only on state law and accuse Microsoft of asking this court to create federal common law in violation of *Erie*. To the contrary, the Ninth Circuit's decision regarding class composition construes the term "employee" as used in ERISA, 29 U.S.C.A. § 1002(6), and the Internal Revenue Code, I.R.C. § 423(b)(4), thereby presenting a federal question. Respondents' SPP claim plainly hinges upon their assertion that they are employees within the meaning of ERISA and Microsoft's ERISA plan documents.[9] Similarly,

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[8] Of course Microsoft made no such sweeping concession but again, even if it had, that would not validate the Ninth Circuit's creation of a right to double benefits for employees of temporary agencies. Respondents hedge their concession argument by alternatively suggesting that, in 1994, a Magistrate Judge conclusively determined that Microsoft was the common law employer of every temporary agency employee who had worked in the past or would work in the future at Microsoft. (Opp'n at 2-4.) Apart from the fatuity of the suggestion that the Magistrate Judge undertook *prospectively* the intensely fact-specific inquiry necessary to determine common law employee status, Respondents' argument fails for the simple reason that, because the District Court rejected the portions of the Magistrate Judge's recommendation that included the finding that the members of the class were Microsoft's employees, the recommendation is without effect. (A35 ("This Court adopted Judge Wilson's recommendations only insofar as they favored Microsoft").)

[9] Respondents offer no support for the suggestion that, because the SPP claim was before the plan administrator when

the basis of the Ninth Circuit's decision to construe the ESPP as having been offered to the freelancers is the conclusion that the ESPP "was an offer to employees, *as that term is defined in § 423.*" *Vizcaino II* at 1014 (A63) (emphasis added). *See also Vizcaino I* at 1197 (A106-107). Moreover, the question presented is not only federal, but it is also one on which a split in the circuits exists. *See Roth* v. *American Hosp. Supply Corp.*, 965 F.2d 862, 867 (10th Cir. 1992) (when confronted with two potential employers, pertinent issue is "*whose* employee was [the individual]"). Far from being irrelevant, as Respondents suggest (Opp'n at 25 & n.18), the pendency of other litigation concerning a temporary employee's common law status further shows the importance of the federal issue presented.

Finally, Respondents' observation that temporary agencies do not offer "duplicate ESPP benefits" (Opp'n at 28), while accurate, utterly fails to answer Microsoft's showing that *Vizcaino III* unfairly permits temporary employees to demand two sets of employee benefits for the same work, although regular employees can receive only one. The temporary agencies do provide, inter alia, 401(k) benefits similar to Microsoft's SPP, which is also a 401(k) plan. As noted by the amici, a ruling allowing duplicative receipt of such benefits has wide-ranging implications for all employers who use temporary agency personnel.

CONCLUSION

For the foregoing reasons and those set forth in Microsoft Corporation's petition, the writ should issue.

Respectfully submitted.

Vizcaino III issued, the Ninth Circuit's determinations concerning the status of temporary employees' common law employment status would not apply to the SPP claims. (Opp'n at 25 n.17.)

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ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

RESPONDENTS' OPPOSITION TO MOTION FOR LEAVE TO SUBMIT *AMICI* BRIEF BY INFORMATION TECHNOLOGY ASSOCIATION, *et al.*

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INTRODUCTION

Respondents oppose a motion for leave to file an *amici* brief by an organization (ITAA) in which petitioner Microsoft Corp. is a major member/contributor. The motion, dated Wednesday, October 20, 1999, was not served on Respondents' counsel until October 28, 1999. The motion is disfavored under Supreme Court Rule 37.2(b).

ARGUMENT

The proposed *amici* brief states it is in support of Microsoft's petition. Proposed *amici* are Information Technology Ass'n of America (ITAA), of which Microsoft is a major member/contributor, and other trade groups. Although Microsoft is identified as a member of ITAA in its website,[1] contributing at least $44,000 per year, the interest of Microsoft in ITAA and Microsoft's contributions to the ITAA brief (direct or indirect) are not disclosed. Supreme Court Rule 37.6; 37.3(b).

The proposed brief sheds no light whatsoever on the principles of Washington state law on which the decisions below were based and which the ITAA purports to address here. The ITAA brief cites not even a single Washington case. The ITAA brief instead proposes, even though this case is governed by Washington law, that this Court should adopt, contrary to

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[1] www.itaa.org/about/members.cfm

Erie RR v. Tompkins, a rule of federal common law to govern this contract claim under Washington law -- *i.e.*, a rule that employers' forms mislabeling employees as "contractors" always control over the facts. ITAA's proposed rule of federal common law is not only contrary to the common law of Washington, it is also contrary to the general common law of agency (see *Restatement (2d) of Agency §220(2)*) applied throughout the United States. See *Nationwide Mutual Ins. v. Darden*, 503 U.S. 318, 322-24 (1992)(adopting general common law for purposes of defining "employee" under federal statutes including ERISA).

The proposed brief should be rejected.

DATED: November 8, 1999.

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